THE MENACE OF MONEY POWER

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To

All Pioneers in the Realm of Thought This Book is Dedicated by One Who has not Feared to Journey with Them in the Quest for Truth

THIS royal throne of kings, this sceptred isle,
This earth of majesty, this seat of Mars,
This other Eden, demi-paradise,
This fortress built by Nature for herself
Against infection and the hand of war,
This happy breed of men, this little world,
This precious stone set in the silver sea,
Which serves it in the office of a wall,
Or as a moat defensive to a house,
Against the envy of less happier lands,
This blessed plot, this earth, this realm, this England,
This nurse, this teeming womb of royal kings,
Fear'd by their breed, and famous by their birth,
Renowned for their deeds as far from home,—
For Christian service and true chivalry,—
As is the sepulchre in stubborn Jewry
Of the world's ransom, blessed Mary's Son :
This land of such dear souls, this dear, dear land,
Dear for her reputation through the world,
Is now leas'd out,—I die pronouncing it—
Like to a tenement, or pelting farm :
England, bound in with the triumphing sea,
Whose rocky shore beats back the envious siege
Of watery Neptune, is now bound in with shame,
With inky blots and rotten parchment bonds :
That England, that was wont to conquer others,
Hath made a shameful conquest of itself.

SHAKESPEARE, *Richard II.*

We, therefore, the Representatives of the United States of America, in General Congress assembled, appealing to the Supreme Judge of the world for the rectitude of our intentions, do, in the Name and by Authority of the good People of these Colonies, solemnly publish and declare,

That these United Colonies are, and of Right ought to be Free and Independent States. . . .

And for the support of this Declaration, with a firm reliance on the Protection of Divine Providence, we mutually pledge to each other our Lives, our Fortunes, and our Sacred Honor—DECLARATION OF INDEPENDENCE, 1776.

The great monopoly in this country is the monopoly of big credits. So long as that exists, our old variety and freedom and individual energy of development are out of the question. A great industrial nation is controlled by its system of credit. Our system of credit is concentrated. The growth of the nation, therefore, and all our activities, are in the hands of a few men who . . . chill and check and destroy genuine economic freedom. This is the greatest question of all, and to this statesmen must address themselves with an earnest determination to serve the long future and the true liberties of men. . . .

We have restricted credit, we have restricted opportunity, we have controlled development, and we have come to be one of the worst ruled, one of the most completely controlled and dominated governments in the civilised world—no longer a government by free opinion, no longer a government by conviction and the vote of the majority, but a government by the opinion and the duress of small groups of dominant men.—PRESIDENT WOODROW WILSON, 1916.

PREFACE

THIS book appears at a time of storm and stress. Political unrest and physical want are manifest. Old modes of thought are losing their sway, new schools are slowly forming themselves. Every aspect of our social, cultural and political heritage is coming under re-survey.

Suspect of thwarting industry, the world's financial system must stand its trial. In its defence it has retained powerful advocates. Its challengers are comparatively unknown. The spirit of justice pleads that the case be heard fully and fairly, and the verdict given without fear or hesitation.

The gravity of the issue can scarcely be exaggerated, as in it are involved the livelihood of the humblest wage-earners and the prosperity of the mightiest nations.

LONDON, *October*, 1921. C. P. I.

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THE struggle between the reformer and the apologist has been long and keen. The progressive type has desired changes in the social structure, while the conservative type thought that, on the whole, the structure was good enough. As the social disease grew worse, the need for remedy became acute, and the inevitability of social reform slowly forced itself upon the public conscience.

The present epoch bids fair to be the most eventful of all history. We have emerged from a great political war, and are entering into a social conflict of which the end is hardly even to be guessed. The reformer has urged the need of drastic remedies to readjust social wrongs, and has succeeded in arousing the public from apathy to interest. His opponents could afford at first to ignore him, but now realise that the contest is definitely going against themselves. Mere conservatism has ceased to be a factor in the social outlook, and all parties present reforms of a sweeping nature.

The reforms proposed all have at least this in

common, that they take away from the individual certain liberties or licenses, and increase the power of the State or corporate bodies. Since the war, it is true, an effort has been made to stress the fact that greater individual initiative will help the economic readjustment. This effort is contrary to the general political trend, and remains without great influence on the minds of the people. The halt which is being called to the activities of the State is due more to the exhaustion of the public revenues than to the positive belief that individualism is in itself a remedy for the social evils.

The increase of the power of the State is not the result of the war. The recent conflict looms so large on our mental horizon that we can with difficulty detach ourselves from it and look back into pre-war days. If we do so, we shall be reminded that even then the economic position of society was not satisfactory. Each political party had its specific programme of reforms to remedy recognised evils. The Conservatives were committed to a scheme of Tariff Reform, the Liberals to a series of alleviating measures, and the Socialists to a wide-sweeping extension of nationalisation or collective control. The underlying method of all three parties was an increase of State interference in industry in one form or another. The Conservative favoured control of the external trade of the country, while

rejecting the same principle in internal trade. The Liberal took up the converse position that the State should extend control and supervision of the internal trade, but should on no account touch the external trade. The Socialist asserted the need for control of the whole of the economic life of the community. It is certainly harder to defend the programmes of the two older parties on the ground of consistency than that of their younger rival. Indeed, consistency cannot be urged in their defence at all. The result is clearly seen in the post-war development. The older parties have followed more or less unwillingly in the wake of the advocates of wholehearted social control. The Liberals have compromised on the subject of control of external industry to the extent of considering modifications of rigid Free Trade. The Conservatives have reluctantly accepted the principle of State interference in wage disputes and of State support for the unemployed. The Socialists have gained strength from the weakening resistance of their opponents, and are proposing further State intervention.

The only consistent opposition put up against the proposals of the three political parties is that of the *laissez-faire* school of thought. This school never wearies of pointing out that the remedies do not cure the disease, but in many cases undoubtedly aggravate it. Their arguments, logical

as they are, fall upon deaf ears. Mere negative criticism is without effect. The reason is that the community has become convinced that an adjustment of the social system is not only desirable, but urgently necessary. It will inevitably continue upon its present experimental lines, unsatisfactory as the immediate effects may be, until all hope of ultimate improvement is killed by the weight of undeniable facts, or until a better constructive scheme is put before it.

The community has, indeed, very solid grounds for its belief that an improvement is urgently needed. Communities are not prone to come to sweeping conclusions except under the stress of great pressure. They do not indulge in abstract thought, but take their ideas from a few selected individuals, often with very little examination. They can be led away by a wave of feeling, but not by an academic principle. The gradual and continual spread of Socialism is due, not to an intellectual examination and approval of its principles, but to a humane desire to escape from what is felt to be an unjust system. The outstanding feature of our social life is that, while the production of the community as a whole has increased to a wonderful extent, the great mass of those who contribute to that increase derive from it little or no benefit. It is not necessary to indulge in idle debate as to whether the workers are better

or worse off than they were in the past. In some respects they are better off, in others they are not so well off. This much is certain, that their lot has not improved at all in proportion to the increase of productive power.* On the other hand, the wealth of those who control industry has increased so rapidly as to be fabulous. The contrast between the penury of the workers and the luxury of the controllers of industry has become so pronounced of late years as to be incapable of concealment except to the wilfully blind. The demand for justice is one of the most insistent of the qualities of man, and that demand is at present not only unsatisfied, but is, it appears, being cheated to a greater extent as the present economic system develops. The need for a greater measure of social justice is the driving force which is taking us for good or evil into the yet unexplored realm of Social Democracy.

Not for the first time in economic history has there emerged a doctrine of hope for the masses of the workers. A century ago a powerful school of thought arose in England. In intellectual ability, in earnestness, in eloquence and in conviction,

* Gide and Rist, p. 342 (see Bibliography): "Statistics seem to show quite clearly that—notwithstanding the influence of powerful factors such as trade unions, strikes, and State intervention—during the course of the nineteenth century, the share of the social revenue which falls to the lot of Capital has increased more rapidly than Labour's."

it could compare with the Socialism of to-day. It has survived simply as a term of disrepute.

The Manchester school of economics has become a synonym for heartless exploitation of human beings in the defence of a soulless principle. Its early triumphs served only to enhance the completeness of its overthrow. It was defeated, not by pure reason or academic argument, but by the irresistible array of facts. Its economic basis is, and has always been, in closer accord with the best teachings of the classical school of economy than the Socialism of to-day. The Manchester school based its arguments upon the teachings of Adam Smith, whose economic reputation is more secure than that of Karl Marx, the apostle of Socialism. The early history of Manchesterism encouraged the greatest hopes of its supporters. Its underlying principle was that an extension of liberty was synonymous with an extension of prosperity and social justice. Its advocates asserted that the worker needed only the freedom to make the best bargain for himself in order to obtain the greatest measure of economic reward. Its philosophic basis seemed unshakable. There could be no thinkable antagonism between those two priceless possessions of the race: liberty and justice. Its economics were equally secure. They were but a logical application of the undisputed principles of the new science. Its histori-

cal environment was most auspicious. Man had achieved the greatest of his triumphs. He had conquered hitherto unsubdued forces of Nature. The power of his hands was supplemented by the use of machines. The end of the eighteenth century witnessed the invention of the steam-engine, which was to enable the worker to multiply his product to an unhoped-for degree. The beginning of the nineteenth century was to see the introduction of the steam locomotive and the steamship, which would help the worker to reach the market that offered the widest scope for his talent and the best price for his produce. The production of the nation was rapidly increasing and the horizon seemed bright with hope.

The earliest victories of the new doctrine only served to confirm the theories of its adherents. The success which accompanied its measures brought in new recruits, until the movement threatened to sweep, in an irresistible flood, onward to the desired goal. Instead, however, of its progress being accelerated, it became more and more retarded. A growing volume of criticism was encountered, which could at first be safely ignored, but which with increasing strength forced itself into recognition. Instead of the machine supplementing the power of the workers' hands, it threatened to supplant the latter. Instead of improved methods of locomotion

aiding the worker to offer his ability and his produce in the best market under the best conditions, it enabled the controllers of industry to produce their goods in the lowest paid wage areas, and to undersell the better paid workers. The manual worker, deprived of an outlet for his wares, was forced to leave his hamlet and crowd into the towns which rose rapidly round the new factory centres. There, the decreasing demand for labour, caused by the growing use of machines, led to an intense competition for employment. The labourer's wage ceased to maintain him in comfort or independence. To supplement it he was constrained to send his children to work for long hours in unhealthy factories. No repetition of academic principles could resist the clamour of the growing misery. The need for a complete or partial redress was overwhelmingly obvious. The criticism of the doctrine of the Manchester school gained in vigour and in volume. It made a direct appeal to the emotions of those who sympathised with the undoubted sufferings of the people, and it won the day.

The Factory Acts were the grave of Manchesterism as a means of reform. The zealous band of reformers of the earlier part of the century had ceased to carry conviction to their hearers, and had commenced to lose faith in themselves. Stalwarts like John Bright fought for their creed to the last.

They failed, not in eloquence or in intellect, but in effect. They were no longer the advocates of reform, but the apologists of an unjust and condemned system. They had promised the people rare and refreshing fruits, which had proved to be withered and rotten. In defence they could only urge that the fruits had had no time to ripen, that competition over a longer period would readjust temporary evils, however acute. Such arguments were wasted on those upon whom the evils were pressing, to whom time was not a philosophic abstraction, but a limited period of life. It was no comfort to a man, whose life was passed in a squalid town, whose children were growing up stunted and underfed, doomed at immature years to work long hours in an unhealthy factory, to be told that an economic principle was working for the certain benefit of his grandchildren. Circumscribed as his outlook was by his misery and his ignorance, it is not to be wondered at that the worker sought relief from his immediate woes by recourse to measures which were opposed to the best economic theory.

The Manchester school ceased to maintain its claim to be the great reforming policy of the world. Thrown back on its defence it soon lost all its old moral fervour, and became the refuge of erudite intellectualism. Its only function at present is to present a perpetual stream of criticism against all

schemes of reform that are put forward from any quarter. As a source of mental gratification its arguments can be read with enjoyment, but they are powerless to check the growing current in favour of economic salvation through social control.

A certain amount of truth must be accorded to the surviving apologists of the *laissez-faire* school. If any function is not necessary in an organism, that function is no longer exercised and will slowly atrophy. The State cannot usurp the functions of the individual without loss to the latter. If the State provides old age pensions the incentive to save for old age is diminished, if not eradicated. If the State builds houses for some persons, others can hardly be expected to deprive themselves in order to buy houses for themselves. The *laissez-faire* school may be right in asserting, as a philosophic maxim, that in any society, other things being equal, the skilful, the industrious, and the provident benefit, while the inefficient, the lazy, and the spendthrift are penalised. As a practical truth, the maxim is of no value whatever, since it completely begs the question at issue. The aim of the reform movement is to bring about precisely that equality which shall allow the better type of mankind to progress, and shall eliminate the worse type. In a society in which it is easy to employ money and difficult to find employment for labour, it is beside the point

to tell the unemployed that they should seek work. It is a truism to say that the unemployment dole will be taken advantage of by the comparatively lazy, and that the moral status of the worker will be lowered.* The main question of the comparative scarcity of employment for labour and comparative ease of employment for money is unanswered. It is unfortunately true that drink leads to squalor and poverty. It is equally true that squalor and poverty lead to drink. Abstract intellectualism that cannot see both the aspects of such a question is out of touch with the facts of life, and will deservedly have little influence on human thought.

If vices were always associated with poverty and virtues with riches, apologies for the present system would be superfluous, and the incentive to reform non-existent. Unfortunately, it appears to the observer that the possession of virtues or vices has little effect upon the general fact that the non-possessing classes have a relatively hopeless lot in life, whereas the possessing classes live luxuriously. The social race is not a fair one. The handicap is uneven, the out-handicapped are clamouring for a readjustment, and have won over the sympathies of the better part of the community.

* Toynbee, p. 105 (see Bibliography): "The whole character of the people was lowered by the admission that they had a right to relief independent of work."

The *laissez-faire* apologist is never tired of asserting that the withdrawal of incentive will cause a diminution of effort. Admitting this to be true, the argument is two-edged. Indeed, it implies an unanswerable indictment of the present system. On every hand there has been a pronounced tendency towards shortening of hours and restriction of output on the part of the workers. If effort and incentive go together, the conclusion is that the present system lacks that very incentive to induce the workers to exert themselves, and is therefore self-condemned. The growing apathy of the worker as to his output is hardly to be wondered at, when one reflects that an increased output does not directly result in improving the worker's status, but simply swells the profits of anonymous shareholders.

History is said to repeat itself. The saying is neither true nor false. Certain historical periods bear some resemblance more or less pronounced to others. In many respects the period through which we are now passing is a counterpart of a century ago. Then as now, Europe had emerged from a devastating war, in which America was also involved. The credit systems of the belligerent countries had become precarious to a degree unknown before. On the other hand, new realms had been conquered by human invention and enterprise. The steam-engine had led to the development of a greater

source of power than the world had ever known. It had brought in its train an increase in the output of coal, which was to be the main feature of the nineteenth century. It was to reduce the earth's circumference from a question of months to one of weeks. It was to eliminate the stage coach and the sailing vessel, and to supplant them by the train and the steamer. It was to make hitherto undeveloped lands a source of wealth.

To-day similar tendencies are at work. The steam-engine is yielding its pride of place as the greatest servant of man. The oil-burning internal-combustion engine has been shown to possess a mechanical efficiency so superior to that of the steam-engine as to make the increasing use of it a matter beyond reasonable doubt. It has induced a production of oil in recent years which is ever increasing in intensity, and has attracted to its service the greatest flow of finance the world has ever witnessed. It has reduced the earth's circumference to a question of days instead of weeks. It has obtained undisputed supremacy of the air. It has invaded the realm of the steam-engine and the turbine on the ocean. It is ousting the locomotive on the railroad. Through the motor-lorry it is already menacing the future existence of the latter. It has given to certain countries a value as a source of motive power which they had never dreamed of possessing

The nineteenth century witnessed a displacement of wealth from the landowners to the controllers of industry. The twentieth promises to see a similar displacement from one section of the controllers of industry to another, from the European to the American continent.

The parallel is not confined to industry alone. It extends to economic theory. Last century received from its predecessor the theory of *laissez-faire*, wrought it into a doctrine full of hope for the people, forced it to the front as a political programme, and witnessed its complete overthrow. The present century receives from the last the theory of social control of industry, has made it a gospel of faith for the worker, has forced the need for its consideration upon national thought, and now waits expectantly for its fulfilment.

Already signs are not wanting of the growth of criticism of the gospel. The evangelists themselves hardly seem so certain as they were. The founders insisted that with the adoption of Socialism the community must progress. Their disciples are asking themselves very searchingly what is the real Socialism. Their former dogmatism is no longer so assertive. Socialism as generally taught some years ago meant quite frankly State or municipal control of enterprise. Now there is a schism in the ranks. The orthodox Socialist still retains

his belief in the gospel. The schismatic accuses orthodoxy of being a method of heartless exploitation of the worker by a soulless bureaucracy, almost the same accusation that was levelled at the Manchester doctrine.

The evolution of the orthodox Socialist is interesting to observe. He loses his guise as a reformer and becomes an apologist. State Socialism has not, he is reluctantly forced to confess, achieved all that he had hoped, but its scope is not yet extensive enough, nor has it had time to make its effects felt. The classes that suffer under its bad effects are by no means appeased by this attitude, and ask themselves what, if anything, is wrong with the doctrine. The doctrinaire section of the dissentients finds an outlet in a reform of the doctrine. Social control is still the gospel, but the ritual is different. Instead of the State or municipality exercising the control, the guild or organised bodies of workers in each industry must do so. Hence emerges the gradual development of a movement among the organised trades to obtain the control of industry, a movement which originated in France and Italy under the guise of Syndicalism, and is spreading in England as Guild Socialism.

The rest of the dissentients have no nucleus round which to form themselves into a new movement and assume the attitude of open or subconscious critics

of the doctrine. Certain general facts are forcing themselves into recognition. Social control, as at present exercised, is not leading to the progress of society as a whole. It is simply enabling certain sections of society to exploit the rest. Manchesterism did no more and no less. It enabled the possessor of the machine to displace the manual labourer and to extort an undue proportion of the produce. It elevated one section of the community and degraded the rest. To-day similar phenomena are taking place and are helped, if not caused, by social control. On the one hand, the financier is acquiring a greater hold upon industry, and is degrading the former independent employer into the subordinate position of manager. On the other hand, the organised workers are using their position to obtain an undue advantage over their unorganised brethren. The unskilled worker is descending deeper and deeper into poverty, and the lower professional and clerical classes are accompanying him in the descent.

The division of society into workers and non-workers is vicious unless a distinction is also made between the privileged workers and the unprivileged workers. This cleavage will probably be one of the important factors in deciding the issue. Manchesterism caused the weight of political power to gravitate from the land-owning to the factory-

owning class. The former avenged themselves by joining hands with the manual workers to pass the Factory Acts, which sealed the fate of the new school. Social Democracy is wresting political power from the employing class, and is transferring it to the skilled Trade Unions. The latter are using it to obtain an undue share of the national production for their members. In the meantime the mass of the community is sinking deeper and deeper into poverty, and may well form a defensive alliance with the employing class.

The Social Democrat is therefore very soon to be thrown on the defensive. He will be accused of favouring one portion of the community at the expense of the growing poverty of the rest. His apology will be that of every discredited system. He will assert that the time factor has not had time to operate, and he will allege that the temporary advantage accruing to the new privileged classes will in time spread over the community as a whole. If, however, such does not prove to be the case—if, on the contrary, the abuse becomes more pronounced as the remedy proceeds—the doom of Social Democracy will be as sure and as unrelenting as that of the Manchester school. The Socialist will have lost his pride of place as a reformer, and will degenerate into the apologist of a discredited system.

Chapter Two: *The Imbroglio of Economy*

No science has less influence upon human affairs than political economy. The teachings of its professors are ignored both by the leaders of social thought and the masses. The stimulus to action has come, not from the knowledge of the orthodox scientist, but from the earnestness of the social reformer. It is strange, indeed, that the science which has as its object the study of the production of wealth has not originated any of the movements which aim at increasing the social well-being of the community. It is not that the community is in such a prosperous condition that the economist is justified in leaving well alone. On the contrary, its condition is unmistakably unhealthy, and, in the absence of any policy from those whose study should enable them to diagnose the disease and indicate remedial treatment, the suffering public turns a willing ear to anyone who has sufficient courage in his own convictions to propose some betterment.

The economist is behind, not in advance of the public, in economical matters. Urgent improvements in our industrial system are necessary, yet the experts make no sign. They continue their

academic studies, they tabulate their statistics, but they do not help humanity. Humanity thereupon takes up the task which they have shown themselves unable to perform and endeavours to work out its own salvation. It is useless for the economist to proclaim that humanity's efforts are misdirected, for the social conscience feels that efforts, however clumsy, are better than inertia. The inspiration which the science gave to public thought in the beginning of the nineteenth century has long since lost its force. Whatever inspiration there is to-day comes from other quarters.

The economist may not consciously realise his lack of prestige. In the lecture-room he may indeed retain it before a small group of students, but in the arena of the world's thought his voice is no longer heard. He has ceased to inspire, and has become to a great extent a codifier of the social trends originated by minds more vital than his own. The result is seen in an increasing lack of confidence, a sense of blind groping in the dark. There is a general inclination to avoid definite conclusions, to refrain from originating ideas; an increasing tendency to wait upon the trend of events, to confine one's efforts to a destructive criticism of the proposals of the layman. It is true that criticism plays an important part in thought, but criticism alone is barren. Creativeness is the

essence of progress, but this faculty seems entirely lacking in the later history of economic science.

The results of the science are the more discouraging when one compares its achievements with those of other sciences. Every science makes its mistakes, and indeed can only progress by correcting such mistakes. Theories are originated and are discarded, new theories arise and are tested. The process is continual.

Whereas, however, we find in other sciences a gradual though uneven progress in the direction of real achievement, in economy we find a mere accumulation of knowledge and unconvincing theory. One has only to visualise the history of the last two centuries to appreciate the striking difference. Other sciences have made immense strides, not only in theory, but in practical application. Doctors have improved their capacity for combating disease, engineers have increased their power of constructing great works, geologists have applied their knowledge of the earth's crust and facilitated our access to its stored-up wealth, but the economist has added little or nothing to our power of dealing with our social difficulties. He has seen the task transferred from his own sphere into that of the politician and the labour leader, and he has supinely accepted the situation.

The conviction of the older economists, erroneous

as it was, was preferable to the hesitancy of the modern school.* Conviction has at least the merit of self-reliance. Lack of knowledge led the originators of the science into many theories which in the light of later knowledge appear to be curious errors. But these theories were consistent with the range of phenomena which then came before the observer, and were preferable as lines of thought to the modern tendencies towards non-committal suspensions of judgment.

The Physiocrat school postulated that land was the sole basis of wealth. It is not surprising that this school should have found its greatest following in France, where the feudal system of land tenure lingered long after it had declined in England. The Mercantile school considered that the prosperity of a country was determined by attracting or retaining within its boundary an increasing quantity of coin and bullion. This concept was, perhaps, partly a heritage handed down from a military to a commercial society. Troops could

* Gide (p. 14), speaking of the historical school, says: "It runs the risk of being purely descriptive. To accumulate millions of facts is useless: there can be no science until relations are discovered between them. If we had to give up the attempt to discover permanent relations and general laws beneath the changing manifestations of phenomena, we should have to give up all idea of making a science of Political Economy. Now, however dangerous to science rash hypotheses may be, they are infinitely less so than such an avowal of impotence."

not very well be paid in kind, so that the kings had always to have available a supply of coin. The more plentiful the money resources of the trading community were, the easier was it for the king to pay his troops. A quaint survival of this theory is seen in the action of the German dynasty in locking up in the castle of Spandau the gold received from France after the war of 1870–71, in order to meet subsequent military requirements. But the Mercantile theory was built upon a sounder basis than mere military needs. History had shown that the feudal system of payment by service or in kind was from the commercial point of view non-progressive. The cash nexus had slowly but surely expanded its scope. Merchants found they could trade upon a cash basis better than on a barter or service basis, and the development of economics supports their views. A sufficiency of cash was necessary for trade, and the standstill caused in a small town if a foreign merchant, by selling his wares, obtained and departed with a large portion of the cash supply was probably immediately obvious. The Mercantile principle was true within the limits of a purely cash basis for industry, but it became less vital when the cash nexus commenced to give way to the credit nexus.

It was left to Adam Smith to give a wider view to the new science. He saw that wealth was not

limited to one or the other of its elements, but comprised the whole sphere of human productivity. When he wrote the credit nexus was slowly imposing itself upon the cash nexus in industry. The development of trade had allowed, to a certain degree, the operation of that great fructifying factor, the division of labour, and the commercial world was full of achievement and hopeful promise. Conservatism in industry, adherence to routine and regulation, distrust of improved methods, inertia—all these were still, as they remain to-day, powerful obstacles in the way of industrial expansion; but in spite of them the commercial system had received an impetus which was to carry it forward into the modern industrial era.

How early in the day Adam Smith made his enlightened observations as to the nature of economic life is not adequately realised. The great inventions that presaged the birth of the industrial era were yet to be made. The cotton trade, in which invention received its first great stimulus, was a minor industry, hardly mentioned in Smith's work. One is apt to imagine that the introduction of machinery stimulated the division of labour. The reverse view is nearer the truth. Only when the division of labour had made fairly substantial progress could men attain the technical skill and the specialised knowledge which enabled them to think out and

construct the machines which were to quicken the rate of progress.

Smith's work was destined to vitalise English political life. The principle of the division of labour implied the liberty for each man to apply himself to that branch of industry best suited to his aptitude. It postulated a fluidity in the industrial system which no State regulations could impart. It brought the desire for political freedom into line with economic progress. Smith's work animated the thought of the nation for a longer period than any other economic writer has ever done. It was the base upon which the Manchester school was, half a century later, to rear its imposing edifice, doomed to collapse in so short a time.

There is a marked tendency in the evolution of all sciences to pass from the construction of theory based upon observed facts into emptier forms of unsubstantial speculation. The danger of aberration from truth in such a process of thought should not be lost sight of. This danger was fated to beset the path of the new science of economy. Smith had drawn his deductions from actual observation; his followers formulated generalised theories without troubling themselves sufficiently as to whether they were confirmed by observable fact. The Manchester school was greatly to blame in this respect, just as other speculative schools of economic

thought are to-day. Manchesterism deduced from Smith's works that the increase of economic liberty should connote the economic progress of society as a whole. When the trend of events showed that the expected development did not take place, the Manchester school did not, in scientific spirit, submit the facts to a re-survey in order to find out whether they had misinterpreted their theory or its application. They persisted in a vain repetition of their speculative doctrines, in spite of the growing impatience of their audience. Their optimistic interpretation of the science of economy showed itself to be unjustified, and a reaction set in.

The history of economic thought in the nineteenth century is that of a struggle between optimism and pessimism, with finally a revival of the historical method. Alternately the Optimists and the Pessimists gained the upper hand, but the triumph lay in the end with the Pessimists. The truth of this is shown by the fact that to-day no influential school of thought holds that economic forces, if left to their undisturbed course, will lead to improvement in the economic structure. But the triumph of the Pessimists has had another result. It has meant that the people has taken the issue out of the hands of the scientists and is determined to work out its own salvation. The scientists have confined themselves more and more to mere historical

research, to a laborious study of economic detail and a registration of fresh doctrines. These doctrines, in so far as they have found any amount of acceptance, have originated, not with the economists proper, but with social theorists from the outside world.

It must not be supposed that the triumph of the Pessimists meant that they were entirely immune from the faults of the Optimists. They shared those faults, but to a less degree. The Optimists indulged in speculative theories. The Pessimists countered by theories not entirely speculative, but based upon a very narrow range of facts. Incomplete as their conclusions were, they were much too strong for the shadowy defence of the Optimists, who in the end succumbed to the successive attacks.

The principal doctrines of the Pessimists were those of Rent, Population, Wages, and Capital. There is a connection between all these. Ricardo's exposition of rent is that in a growing community rents will rise, profits fall, and wages remain constant. Malthus went further and pointed out that by natural laws population tended to outstrip food supply. He also postulated the existence of a wages fund which, though capable of being added to by saving and increasing with greater wealth production, was at any given period practically a fixed

amount. The average wage of the workers was therefore obtained by dividing the number of the latter into the total wages fund. Any increase in the number of the workers tended to decrease their average wage. This theory was also held by Ricardo, who thought that, as population was increasing faster than capital, the lot of the labourer was a worsening one.

The doctrines of Ricardo and Malthus were not at all heterodox. They became the established tenets of the orthodox school. Their attitude was one of frank helplessness and hopelessness. Society as a whole was making a wonderful effort. Its productivity was rapidly increasing. Yet the lot of the labourer was, by immutable iron laws, innate in the very scheme of social relations, doomed never to improve. Increased production in agriculture would be met by higher rents, increased production in industry would hardly affect the wages fund, and the tendency of the population to increase in geometrical progression would keep the lower classes on the poverty line.

Ricardo and Malthus defeated the Optimists because they used more powerful weapons. Their theories fitted in with the observed facts of the time. At that period a big increase in population had taken place; the purchasing power of the agricultural labourer had remained steady just

at a point where he had a hard struggle for existence. The purchasing power of the trade worker had fallen rapidly from 1750 to 1820 owing to a great rise in prices, and the conditions in the factory towns were so appalling that the public conscience was deeply stirred. While the Optimists were expounding their well-worn academic principles, the people were turning their ears to those whose theories were more in accord with the prevailing conditions.

Instead, however, of the Pessimist doctrines lulling the masses into a feeling of dull resignation, in the long run they defeated their own ends. In a stationary Oriental system resignation is a dominant trait. With the progressive races of Western Europe such a quality has little place. Mental processes are subconscious before they are conscious, and a subconscious feeling of rebellion soon manifested itself. The expression of that rebellion was at first incoherent. It found its utterance in works like Carlyle's *Past and Present* (1843) and Hood's *Song of the Shirt;* in various tentative and sporadic attempts to start small idealist centres of production upon communal and co-operative lines. It essayed political reform through the Chartist Movement (1836–48). Finally, the doctrines of the Pessimists were seized upon by the powerful thinkers of the reform school, intensified and

used, not as a narcotic to lull society to apathy, but as a weapon with which to attack its whole structure.

Ricardo's theory of rent was based upon observations of the earlier part of the industrial era, and dealt with farm-land, agriculture being then more important than all the other industries combined. The growth of the towns brought into prominence the fact that the profits of industry were also liable to exploitation.* The principle of rent was so disastrous in its logical application that the only hope for society was to overthrow it or to divert the revenue from it to the public good.† This was ably advocated by Henry George in his *Progress and Poverty* (1881). Since the landlord increasingly exploited the community, the latter was justified and well advised in forcing him to give up his unearned gains to pay for the increasing public expenditure. These ideas have to some small extent been embodied in British legislation. Even to this day, however, the teachings of Henry George have not secured the general allegiance of public opinion.

* Professor Cairnes, *Leading Principles of Political Economy*, 1864, p. 333: "The large addition to the wealth of the country has gone neither to profit nor to wages, nor yet to the public at large, but to swell . . . the rent-roll of the owners of the soil."

† Roesler, *Grundsätze*: "Political Economy would only be a theory of human degradation and impoverishment if the law of rent worked without modification."

The more formidable champion of the submerged was Karl Marx. Before him Rodbertus and Lassalle had attacked the wages theory, the "iron law" which Lassalle so aptly dubbed "the brazen law of wages." It was left to Karl Marx to make the law the basis for a comprehensive attack upon the industrial system. He set himself to prove not only the truth of the law and its inevitableness, but also its progressive effect. The evolution of the capitalist régime meant the continuous degradation of the worker, the accumulation of wealth into fewer hands, until by the very force of circumstances humanity, dispossessed of its natural heritage, would at last despoil the despoilers and wrest back the whole economic system to be administered henceforward under common control. From that day to the present time his doctrine has gained an increasing number of adherents, and all political movements have been forced to bow to a greater or less extent to its influence.

It must be pointed out, however, that there is an inherent discrepancy between the Georgian and Marxian doctrines which cannot be overlooked. The one maintains that the surplus product tends to go to the landowner, the other that it tends to go to the capitalist. The Marxian doctrine is nearer the truth. There appears ample evidence that the dividend-receiving class is a larger benefiter

by the present industrial system than the rent-receiving one. It is true that some landowners are enormously wealthy, but they are indigent compared with the great financiers. Furthermore, political power has gradually migrated from the landed to the industrial interests. The popular mind, at any rate, appears to have no doubt as to which of them are the greatest exploiters of the community, and, in so far as it concerns itself with remedying the matter, is undoubtedly on the side of the Marxian doctrine. The fact, however, that these doctrines cannot both be right in their entirety leads us to enquire whether they may not both be incorrect.

To revert for an instant to Ricardo, it will be seen that his theory of rent is not a theory of the nature of rent at all, but a theory of maximum rent. It deals with quantities, not moral rights. It deals not with the reason why the user of the land consents to pay over a portion of his product to one who, in simple character of landowner, is a non-producer. It concerns itself only with the greatest value which that rent can bear to the total product. Rent in its earliest origin appears to have been partly a payment for the acknowledged service of protection, partly a forced levy exacted by the military members of society from the weaker land-users. In the first place, it was a kind of

crude insurance; in the second, an act of extortion palliated by the low level of social ethics. Before the introduction of the cash nexus, it had to be paid in kind or in service. Such a system was too inelastic to admit of a maximum payment of rent. The rent payable was determined largely by custom, but the difficulty of subdividing service and produce made it hard for the feudal lord to exact the uttermost from his inferiors.

The introduction of the cash nexus led to a loosening of mutual feudal ties, and, by its greater fluidity, induced a more elastic method of bargaining in which the feudal owner stood to gain. At the same time the political institutions of the country, dominated by the land-owning classes, transformed a feudal claim to possession into a legal claim which has never been effectively challenged. Competition for the possession of land upon the basis of a legal claim which allows of absentee landlordism has tended to enhance the rent value of land. The maximum rent of the Ricardian theory is, however, far from an economic reality, since, if it were, the landowners should have appropriated to themselves the whole of the community's increased wealth, which is not the case.

While, however, the political system was perpetuating in legal form the old claim to rent based upon feudal obligation, the silent play of natural

economic forces was working towards a system of occupying ownership.* It may be argued that occupying ownership would still leave the land-owner in a privileged position with regard to the industrial and agricultural workers. It would, however, eliminate him from social life as a non-productive burden upon industry. Moreover, it should be borne in mind that land-rent is not the only form of rent that increases in a modern community. The modern economist has pointed out the application of the principle to mines, fisheries, and manufactures.† It is true that the value of land tends to increase according to the number of persons who are dependent upon it for food. But so does the value of a business increase with the number of its potential customers. A small village shop has a limited profit-making

* Toynbee, p. 129: "Sir H. Maine and M. Laveleye, for instance, have taken an historical survey of land tenure, and drawn from it the conclusion that the movement of property in land is always from collective to individual ownership, and Mr. Ingram again, alluding to this law, accepts it as true that there is a natural tendency towards private property in land. He can build his argument on the universal practice from Java to the Shetlands, and it would seem a legitimate conclusion that the tendency will be constant."

† M. Beer, *A History of British Socialism*, vol. i., p. 151: "Had Ricardo thought out his theory of marginal labour to its last consequences he would have come to the conclusion that the profits of all better equipped manufacturing establishments also partook of the nature of rent."

capacity. An establishment in a large town is potentially and usually a source of greater profit. The surplus profit-earning capacity of the latter is due to the larger number of persons who look to it for their supplies, and is, in effect, a type of industrial rent, part of which is now expropriated by the absentee landowner. Still lower in the scale, the worker in a populous district enjoys a certain surplus value over the village labourer in the facilities and the amenities of social life. This increased value due to a denser population is in itself not necessarily a defect, but should be an asset to the community, if the value were fairly distributed. Under absentee landlordism, however, the non-producing class benefits unduly. The natural tendency towards occupying ownership is a tendency towards the elimination of the gravest defect of the present rent system.

Malthus' original theory of Population, in its extreme application and without any of the provisos subsequently added to it, is as irreconcilable with the doctrines of Henry George and Karl Marx as the latter are with one another. It precludes the possibility of surplus product either as rent or capital. It postulates an inherent tendency in the population to outstrip the means of subsistence. If that tendency operated to the maximum degree, with no counterbalancing check, it would mean that

the whole produce of society would be necessary to nourish its members. There could be no saving of product at all, either to be handed over as rent to the landowning class or to be used as capital to promote production. The wealthier members of the community would simply demonstrate their wealth by having a greater number of children. Malthus wrote his treatise at a time when the population was increasing rapidly and when the rising prices called attention to the growing scarcity of commodities. He then saw only the positive check to population resulting from actual want, but in a later edition of his work he admitted a preventive check in prudential restraint. The admission destroys the argument. In primitive societies undoubtedly the positive check was the only one, but the prudential check has made itself increasingly felt. Naturally enough it has shown its influence at the upper end of the social scale more than at the lower end, but even there it is not entirely absent. The fact that the marriage rate was observed by Malthus to follow the price of corn was an argument against his theory, not for it, because it meant that even the poorest, instead of blindly rushing into marriage, were to some degree exercising prudence. The same qualification applies to the Malthusian as to the Ricardian theory. It is a theory, not of population, but of maximum population. It seemed

quite convincing to the generation for whom it was written, but has long since lost its value. Its force wanes as we pass from primitive to industrial society. In the most highly organised societies of the present time the danger comes, on the whole, from the opposite direction. There is a great tendency towards diminution of population. France has already passed its highest point. England appears to be approaching it. America increases its numbers, not from its native-born citizens, but from immigration. The law of population must be stated in quite different terms from those of Malthus, and it would appear that the tendency towards propagation in any society bears some kind of inverse relation to the amount of surplus product.

The most influential of the writers of the Pessimist school is Karl Marx. He saw no hope in the modern industrial system as such. He visualised it as tending, by uncontrollable inherent forces, to its own doom, to make place for a new system of social democracy. He was, however, not a complacent Pessimist at all, no mere apologist of the old order, but an apostle of the new. He threw down his challenge to the defenders of the industrial system. At first they ignored the challenge, but finally they have had to take it up, and now find themselves on the defence against the growing army of the followers of Marx. The Marxian doctrine has in its general terms

become familiar to all. It is to the effect that the competition between the worker and the capitalist is an unfair one, the former having only his labour-power to offer, whereas the latter possesses the means of production. The result is that the latter is in a position to drive a bargain in which the former must work for a subsistence wage only, all his surplus product going to swell the profits of the capitalist. The almost mathematical means by which Marx attempted to show how the surplus value was extracted from the labourer has already encountered much criticism, and that part of his teaching now appears to have lost its hold upon all except the extreme doctrinaire wing of his followers. Whether his actual demonstration of the process was correct or not, he is not wholly wrong in his statement of the effect. That the labourer is exploited of the whole of his surplus product is an overstatement. His subsistence wage is allied to his standard of comfort, and as that standard has shown itself to be a variable one, the Marxian doctrine cannot be rigidly applied. But Marx was correct at least to this extent, that an unfair proportion of the produce goes to the non-producing class, and his contention is borne out by appeal to economic facts. Marx went further and pointed out that the "capitalist" system would lead to an increasing accumulation of capital in the hands of a few. The ultimate

outcome of "capitalist" society, if left to pursue its course unchecked, would be the division into two defined camps—a large mass of expropriated proletarians on the one hand, and a decreasing number of increasingly wealthy "capitalists" on the other. The only solution to such a position was for society as a whole to reassume the control of industry for the benefit of its members.

It is interesting to mark a similarity between the gospel of Marx and the old Hebraic doctrine of original sin. According to the latter doctrine, mankind is, as a result of an original slip, inherently sinful, and can only be saved by the coming of a Redeemer. The Marxian conception of economics is that capital, a product of human endeavour, is inherently vicious and is steadily luring society to its downfall. Salvation can be effected only by the advent of all-redeeming Socialism. It is not surprising that such a solution should have appealed to a thinker of Hebrew origin.

It should be borne in mind that, at the time that Marx wrote, the industrial system had not developed to such an extent as it has to-day. Marx saw its results more or less clearly as they then divulged themselves. The medieval craftsman, possessor of the instruments upon which his livelihood depended, to some extent also the producer of his own raw material, had given place to a worker

whose sole possession was roughly his labour power. Capitalism, as Marx understood it, had dissociated the worker from his tools. But the Marxian concept of capitalism is not satisfactory. So much abuse has been poured upon the so-called capitalist system, and all hopes of social regeneration depend so entirely upon a correct concept of what is implied in that term, that a clearly defined idea of capital is a matter of vital necessity. Our longer perspective of the development of industrial society has revealed to us the emergence of another class in the economic structure, the financier class. In the days of Marx the capitalist was still to a very large extent both owner and user of the means of production. The factory had displaced the craftsman, and the machine worker had supplanted the tool worker. The capitalist was the direct controller of the factory. Nowadays that is no longer the case. The system which dissociated the worker from the ownership of tools has dissociated the ownership of the factory from its management. The former capitalist has been degraded into the position of technical or business manager. He is no longer a freeholder, but a leaseholder. The factories have passed from the ownership of the capitalist into the ownership of the financier.*

* Gide and Rist, p. 463: "Under the joint stock principle the right of property is simply reduced to the possession of a few strips of paper giving the anonymous owner the right to draw dividends in some commercial concern or other."

The terms "capitalist" and "financier" are confused in the popular mind, as are the underlying ideas of capital and finance. Marx himself realised that the birth of capitalism synchronised with the emergence of money as a factor in the economic organism,* but he made no clear distinction between finance and capital. On the contrary, he accepted them as synonymous terms. Nevertheless there is a wide divergence between capital as such and finance as such, and the understanding of that difference is vital to the correct solution of the social problem.

In the light of these considerations the Marxian concept of economic development needs restating. The introduction of money into the commercial organism imparted to it a fluidity which enabled capital to be built up. The industrial era saw an immense development of capital which helped to increase the productivity of society. It saw the introduction of the steamship, the railroad, the factory, vast engineering works, and other triumphs

* Karl Marx, *Das Kapital*, Part II., chap. iv., p. 123: "The circulation of commodities is the starting-point of capital. . . . If we abstract from the material substance of the circulation of commodities—that is, from the exchange of the various use-values—and consider only the economic forms produced by this process of circulation, we find its final result to be money: this final product of the circulation of commodities is the first form in which capital appears."

of industry, all parts of that constructive mechanism which should have helped towards a better state of society. At the same time, however, upon the basis of money there was being erected a system of finance the workings of which have not yet been sufficiently critically examined. The earlier phases of the financial system had the obvious effect of reducing a large portion of the craftsman class into toolless workers dependent upon the employers for their wages. The later phases of finance have seen the growth of a credit nexus, which has already, to a large extent, reduced the direct employer of labour from his erstwhile independence to the position of salaried worker for financial bodies.

In spite, however, of the searching criticism which has been devoted with growing intensity to the examination of the economic structure, the fundamental evil appears to have escaped observation. The question of finance is held to be too intricate for the lay mind, and the pronouncements of the financiers themselves are taken as final. It is too much to expect that any hierarchy should condemn the creed to which it owes its exalted position, and it is therefore not surprising to find that the financiers have not condemned the structure which gives them their pre-eminence. Though the dicta of *ex-parte* advocates have secured for our financial system complacent acceptance and

even admiration in the past, a change of view is coming into evidence. The facts of the case are slowly forcing themselves upon the public mind. The colossal fortunes amassed in recent years have been made, not by men directly engaged in the production of wealth, but by those who have had sufficient knowledge of the working of the financial system to enrich themselves by the labour and technical skill of others. The Great War has called attention to the dependence of the masses of the people upon the financial situation. All proposed schemes of economic reform seem doomed to abortion on account of the exhaustion of means of financing them, and attempts to reconstruct the communities of Eastern Europe upon the lines loved by the doctrinaire reformer are threatened with complete failure owing to the collapse of the new economic order founded upon an insecure financial basis. The time would therefore seem to be at hand when it is possible to hope for a reconsideration of the financial basis of the economic structure upon the lines of open-minded criticism. In order to get a clear conception of the problem it is necessary to trace the development of the modern industrial society from the earlier feudal form through its successive stages, and to try to foresee to what goal it is speeding. Then only shall we be able to attempt a solution of the social problem.

Chapter Three: *From Feudal Status to Cash Nexus*

THE difference between the feudal and the industrial systems of society is in the main the difference in the nature of the dependence of the bulk of the people. In the feudal system the masses were bound to the soil, which was owned by a comparatively small number of feudal lords. The mass of the people was divided into freemen, villeins, and serfs. All these were dependent upon the land for their subsistence, and owed varying amounts of service to their feudal lords.

The loosening of the feudal bond is allied to the gradual infiltration of cash payments into the social organism. This process was of slow but insistent growth. The feudal servant's obligation to pay his dues in labour or in kind was gradually dissolved, and, instead, he had to pay a money rent. Concurrently it became possible for the masses to free themselves from direct bondage to the soil, but in so doing they became increasingly dependent upon the necessity of earning a wage. So marked has that dependence become that it has had applied to it the picturesque term "wage-slavery", not wholly without foundation. Undoubtedly for the great mass of people to-day the prime feature of

economic life is the necessity of earning a wage, just as in the feudal system the prime necessity was to obtain the use of land from the feudal lord.

The study of the emergence of the cash nexus is an important preliminary to a correct grasp of economic problems. Money has existed in all societies in which any kind of trade as distinct from primitive barter was carried on. In early societies a money transaction was a rare event, the hunting or agricultural pursuits of the community being the real basis of communal life. Thus in African tribes we find cowry shells used as money; among the American Indians, skins of animals. In more highly organised societies the dominant form rapidly became some metal or other, until it was more or less replaced by paper currency.

The use of metal as currency goes far back into the agricultural era. Etymology shows that prior to the use of metal the exchange of commodities was made upon the basis of their worth in live stock.*

With the development of society and the increase of the use of metals the latter replaced cattle as the money instrument, and at different stages iron, copper, silver, and finally gold were adopted as

* Pecuniary, from Lat. *pecus*, cattle. Fee, feudal, from A.S. *feoh;* compare German *vieh*, cattle. Cattle, chattel and capital are all from the same root as Lat. *caput*, a head.

cash. The Greeks, Phœnicians, and Romans all developed a considerable amount of commerce which was conducted upon a cash basis. Under the Roman régime the process went a step further, and led to the introduction of the credit nexus in the form of the bill of exchange. The decay of the Roman Empire under the successive onslaughts of the semi-barbarian tribes arrested the growth of commerce, and produced an interval of unsettlement which later gave way to a period of stability under the form of the feudal system. The precarious conditions of the time led men to seek security by attaching themselves to a strong military leader, whose protection they obtained in return for service. That system developed on the Continent to a higher degree than in England, whose insular position afforded it a certain amount of protection. But the invasion of the Continental tribes, the Angles and Saxons and later the Danes, helped to stimulate the feudal system of land tenure, and the great conquest by William of Normandy gave the system its dominating character.

Feudalism, however, was at no time entirely free from an overlayer of commerce conducted upon a cash basis. The feudal lords had a direct interest in encouraging a certain degree of trade. They needed, to uphold their position, a high degree of craftsmanship in the manufacture of

weapons and armour. They required the merchant to supply them with fine apparel. The technical skill of Europe was insufficient for their highest requirements, and they sought their weapons and their textiles from Damascus and other Asiatic cities. Such commerce was, however, but a superficial manifestation of feudal life. The great mass of the people was to all intents and purposes self-supporting, and the exchange of commodities, with its concomitant use of money, rarely entered into their lives. The typical illustration of feudal life is to be found in the feudal villages scattered far and wide over the country-side, not in the rare towns which rose up where the craftsmen congregated or where the caravan routes made convenient merchant centres.

The feudal village consisted of a few houses clustered along the village street near the manor of the feudal lord. The villagers held their land in servile tenure from the latter, and in return for their holdings had to work for the lord of the manor for a fixed number of days per week throughout the year, and for a fixed period during special seasons such as ploughing and harvesting. They were unable to leave the village without first obtaining their lord's permission. They were classed generally as villeins, and were subdivided into virgaters or cottars in accordance with the size of their holdings. A vir-

gater was a holder of some thirty acres, a cottar had some five acres only. In addition to the labour rents, they were compelled also to give other rents in kind, such as corn or honey. Above them in the social scale was a small body of freemen, who were on the whole exempt from labour dues, but who were still under the obligation to pay rents in kind. At the other end of the scale were the few bondmen or serfs, who held no land and were wholly dependent upon the feudal lord.

The land of the village was divided into permanent pasture, waste, wood, and arable. The pasture was used in common by the lord and the tenants. The wood provided them with timber and fuel. The waste land fed the swine. The arable land was worked on the open-field system. The fields were divided into strips some eleven to twenty-two yards wide. These strips were divided among the lord and the tenants, and each man's holding was scattered in this way over the whole of the manor lands, no two adjacent strips belonging to the same man. Each village had two or three such fields. In a three-field village, one field would lie fallow each year, while, of the other two, one would be put under barley or oats, the other under wheat or rye. In addition to his strips in the open field the lord had also some enclosed fields near his manorial hall. His holding in both strips and enclosed

fields was called the demesne. The feudal lord, particularly after the Conquest, held several possessions in various parts of the country, and it was his custom to place his lands under the control of the bailiff. To plough the demesne, the tenants combined their oxen into teams of eight, and also to some extent made use of this practice in ploughing their own holdings, although individual ploughing was probably more common.

The villagers lived almost entirely upon their own produce. They possessed their few oxen and swine, raised upon the common pasture and waste land. They got their timber and their fuel from the wood. They prepared their own leather and wool. Each village was practically a self-contained unit, except for a few commodities such as iron, other metals, and salt. Sugar was unknown, and its place was taken by honey. In the early days of the system the king was merely a superior feudal lord and lived upon the produce of his lands, like his vassals.

Such a system, primitive as it was, might appear to have the elements of permanency in it. A change, however, was destined to intrude very gradually and to end by converting the feudal system into the modern industrial one. The impetus to change came in the first place, not from the striving of the tenants, but from the needs of the feudal lords. While it would appear that the tenant's position

in such a system was by no means an enviable one, there does not appear to have been any noticeable discontent. True, the tenants were at the lord's mercy and, when he abused his power, their power of redress was practically nil. But the affairs of the community were controlled rather by traditional regulation than by despotic power. The tenant had certain claims by reason of his class position. His duties to his lord were prescribed by usage; he was by nature conservative, and showed no desire to upset the social structure.

The feudal lord's needs were not so easily satisfied as those of his tenants. He owed his position to his prowess as a fighter. He needed good weapons, good armour, good horses. His prestige necessitated better clothing than the village could provide. He had duties to his overlord. Upon occasion, he had to accompany the latter to battle and bring with him a body of fighters. While he could support his retainers at home upon the produce of his lands, the system failed when he took the field. The provisioning of even a small army could be better effected by the purchase of necessaries than by forcible extortion. Even in times of peace, the fact that he possessed several fiefs at long distances from one another made it to his interest to introduce a more convenient system than that of labour and produce rents. He was more detached from the primitive

product of his own lands than were his tenants, and he was acquiring a growing attachment to the products of commerce.

What held true of the feudal lord held true to a greater extent of his overlord, the king. The king had a still greater state to keep up. He had a larger retinue to clothe. He had Continental possessions which, by intermarriages, in course of time came to include the best provinces of France. He had to support an army and to be able to provision it. It was easier to buy food wherever convenient than to transport it from his own domains. To do that he stood in need of money.

The decline of feudalism is the history of the commutation of labour and produce dues into money rents. This process is naturally earliest in evidence in relation to the larger domains. Up to the reign of Henry I. (1100–35), the produce of the royal manors used to be sent direct to the King's court, but the method of marketing them close at hand and sending the money received to the king was much more convenient for all parties. The larger estates followed on the same lines. The Church adopted the practice.* Early Church history affords

* Ashley, p. 46: "The transition from payments in kind to payments in money, which, on the manors of St. Paul's Chapter and doubtless on those of many other ecclesiastical corporations, was delayed until the fifteenth century, had upon the royal demesne taken place early in the twelfth."

records of detailed arrangements for provisioning monasteries direct from manorial produce. This was later replaced by the commercial method of sale and purchase. On the smaller demesnes the enterprising bailiff could better satisfy his ambitious lord by letting land out for a money rent instead of for labour and produce dues. When, however, the relations between feudal lord and tenant were direct, natural conservatism prevented the change from developing, except at a very slow rate. The infiltration of the cash nexus throughout society was not destined to be direct from feudal lord to tenant. It was rather from feudal lord to merchant, from merchant to craftsmaster, and from craftsmaster to journeyman. It led to a growing increase in the town population and a growing interdependence between town and country-side. Produce rents were not practicable for town dwellings, and were early supplanted by money rents. The growth of the towns gave the country-side a profitable market for its produce. It made the tenant's produce and labour a source of gain, and gave him an incentive to produce for sale instead of for subsistence. Thereby it increased the tendency towards holding land on lease in return for money rent. The old system of tenure was, however, very persistent, and remained until the commercial system had superseded the agricultural.

The merchant emerges in economic history at first as a trader dependent upon and subservient to the feudal lord. He traded in a small way with the inmates of the feudal castle. The growth of the religious orders enabled him to attach himself to some high Church dignitary. As the need for the merchant became greater, towns sprang up in the neighbourhood of the large castles and monasteries. The merchants were general traders. They dealt in the native products, which comprised wool, rough cloth, leather, and food, and also imported products, such as finer cloths, silks, furs, arms, spices, and wines. The feudal lords were jealous of their position and were not inclined to give the merchants any special privileges. The advent of the Crusades, however, gave the merchants an opportunity which they were not slow to seize. The feudal lords stood in urgent need of money in order to equip themselves for their pious ventures. For a certain fixed sum the merchants were allowed to purchase their charter of freedom. The granting of the charter was followed by their organisation into a gild merchant, which gave them sufficient solidarity to defend their purchased privileges. The gild merchant secured for its members the sole right to trade in their town.

It is not surprising to find that the development of the English towns was to a large extent copied

from towns on the Continent, nor that throughout the whole of the Middle Ages the commercial development of the Continent was generally ahead of that of this island. The causes which operated at home in the direction of fostering the growth of commerce operated to a greater degree abroad. The interests of the Continental feudal lords were wider, their quarrels were more frequent, their need for money to maintain armed forces was greater. Their dependence upon the merchant was therefore more marked, and the Continental merchant was in a better position to obtain a privileged position. Hence the Continental towns assumed a commercial importance at an earlier date.

In England those towns more happily situated for Continental trade made the greatest progress, and it is in them that the gild merchant was first incorporated. Thus the merchants in London and the Cinque Ports at an early date obtained trading privileges, though they appear never to have troubled about the actual formation of a gild merchant. The first gild merchant was formed about A.D. 1100, and the number increased rapidly until the height of their development was reached in about A.D. 1300.

The rise of the merchant brought with it the creation of the craftsman. The more skilful manual worker of the village found it to his advantage to

free himself from the land, with its labour and produce dues, and sell the products of his craft to the merchant or to his fellow-villagers. The further penetration of the cash nexus into the social organism led to the formation of another industrial stratum. Specialised crafts developed quickly in various towns, and very soon after the formation of gilds merchant we find craft gilds springing up. Before the actual separation of craft gilds from gilds merchant, the latter included craftsmen among their members, but regulations were introduced to limit the craftsmen's activities. No craftsman could sell his wares outside his own town, which meant very largely that he was obliged to sell to a merchant. To become a merchant he must first give up his craft and sell his tools. The attempt on the part of the upper stratum to protect itself from the newer and lower stratum is one which we shall see repeated by the craftsman against the journeyman. The first evidence of a craft gild is in 1130, and is in the cloth industry, the weavers having then organised in London, Lincoln, and Oxford. Shortly afterwards fullers and cloth finishers, goldsmiths and butchers, formed themselves into gilds in various towns, and the movement continued to gather strength until about 1350. It maintained its vigour for about a century till 1450, and then slowly declined.

In the early days of the craftsman it was comparatively easy to obtain the necessary skill, and the outfit required to set up in industry was not expensive. The market was very circumscribed, being usually limited to the town itself and the surrounding rural district. Inter-urban commerce was carried on by the merchants. The profits made by the craftsmen, although not great, were sufficiently attractive to cause an inflow of new members. Competition began to make itself felt, and when the craftsmen found their profits being undercut by the growing competition they organised themselves upon restrictive and protective lines. The increasing specialisation of craft led to the development of sufficient technical skill to justify the introduction of the apprenticeship system, the first evidence of which is in 1260. This system was soon used to restrict the numbers of those entering a craft. An attempt to meet this evil was made by legislation, and in 1531 an Act was passed fixing the maximum fee for apprenticeship. As early as the fourteenth century, however, certain craft gilds had made regulations to limit their numbers, to restrict output, and to inflate prices. The lure of the more profitable cash commerce was seducing the peasant from the soil, and in 1406 an Act was passed to prevent men whose incomes were less than £1 per annum from apprenticing their children in the towns.

Steps were also taken by the more influential members of the gilds to get the control into their own hands. They fixed the hours of the gild meetings at difficult times, and ordained the wearing of costly liveries. The term of apprenticeship was lengthened to seven years, the number of apprentices were limited, and every endeavour was made to render the gild practically a hereditary monopoly. Even at the end of his term the apprentice was no longer certain of becoming a craftsman. In order to qualify he was obliged to produce a masterpiece. This masterpiece was first instituted as a test of skill, but later degenerated into a means of exclusion. The work required was of such a character as to necessitate much expense, with the object of keeping out the poorer class of worker. The result was that the apprentices who could not qualify as craftsmen slowly became a new class of journeymen, condemned to work for a wage for the wealthy members of the craft. The journeymen in time became so numerous that they formed themselves into associations. They are the forerunners of the wage-earning class, the ancestors of the modern proletariat. Their attempts at organisation for protection were not to the liking of the municipalities, which were controlled by the gilds merchant and the craft gilds. The earliest evidence of this development

is in London, where in 1303 the cordwainer journeymen were refused permission to make ordinances for themselves. From that time onward the growth of the journeyman class was very rapid, and the different associations which rapidly sprang up afford evidence of the extent to which the division of labour and the specialisation of craft had progressed. In the latter half of the fourteenth and during the fifteenth century, journeymen associations were formed of saddlers, cordwainers, tailors, blacksmiths, carpenters, drapers, and ironmongers. In the sixteenth century, founders, fishmongers, clothworkers, and armourers were added to the list.

Three strongly characterised industrial and trading classes—the merchant, the craftsmaster, and the journeyman—had developed therefore out of the feudal system of lords and tenants. The apprentices did not form a distinct class, as their function was to develop at first into craftsmasters, but later increasingly into journeymen. Whence did these classes trace their source? Not from the feudal lords, since it is only comparatively late in the day that we find the cadets of noble families, the De La Poles of Hull and others, embarking upon industry. The recruits of industrialism were drawn from the tenant classes, from the freemen, the villeins, and the serfs. The Act of 1406 refusing apprenticeship to sons of men whose income was

less than £1 per annum shows that a trade career had offered an avenue of escape from the soil even to the poorer grades of tenant.

The infiltration of the cash nexus into feudal society had up to this period, on the whole, connoted an increase of freedom and economic well-being. Counter-currents were not wanting, it is true, and the flow from fixed status to freedom was by no means devoid of them. Those currents will be found to grow in force later on until the promised freedom will turn to an economic pressure akin to thraldom. This trend will, however, not develop until the cash nexus shall have yielded to the credit or finance nexus. The tenants, then, freed themselves from the soil and migrated to the towns. The resultant growth of the towns in size and in power is a feature of the period from the thirteenth to the fifteenth centuries. Civic authority passed from the hands of the gilds merchant to those of the craft gilds, not without a fluctuating struggle. Civic rights were secured by a charter of incorporation. These charters were given by the kings grudgingly, as they were held to be an alienation of royal powers. But the king's necessity or his ambition proved the road to civic freedom. Henry II., for instance, snatched at the crown of Sicily for his son in 1255, and found himself embroiled in an expensive foreign policy. To

this fact may be traced the grant of many borough charters:—Norwich, Nottingham, Northampton, Lincoln, and Lynn in 1255; eight further ones in the following year. But the gild authorities used their powers, not only to secure their freedom, but artificially to protect their industry. They introduced regulations to control prices, hours of labour, influx of apprentices and journeymen. The passing of power from the gilds merchant to the craft gilds freed the merchant from his dominating urban interests, and his search for gain led him to develop new avenues of production. Open-field cultivation was slowly giving way to enclosed-field cultivation; arable land was being turned into pasture, and the wool clipped from the sheep was supplying the material for England's great staple industry.

The woollen industry was one of the oldest in England, already well developed in the twelfth century. It then declined, but regained prominence in Edward III.'s reign (1327–77) partly owing to the encouragement given to Flemish weavers to settle in England.

The decrease of arable meant at first the depopulation of the country-side, and the growth of sheep farming (1500–50) led to many bitter complaints. Legislation endeavoured to check it, with indifferent success. Poor Law measures to relieve distress were framed, at first on a voluntary

basis (1531), afterwards to be made compulsory (1563). After many years, however, the sheep runs were to deal a hard blow at the towns, those protected corporations which seemed so secure in their privileges.

The struggle between the towns and the countryside is connected with the rise of the clothiers—the merchants who specialised in the staple industry of the country. The clothier is regarded as the forerunner of the modern capitalist, but can better be looked upon as the primitive financier. In the early days of the merchant class the inequality of fortune was not greatly pronounced. The gilds merchant had some of the aspects of communism. An early privilege of the gild member was that of sharing in any bargains made by a fellow-gildsman. This privilege was modified later on, but would certainly tend to equalisation of profits. It was only on the decline of the gilds merchant that evidence of huge fortunes in the merchant class comes to hand. In 1363 a London vintner was of sufficient prestige to feast four kings, while in 1460 William Canynges, a clothier of Bristol, entertained Edward IV. In 1339 Thomas Blanket of Bristol is cited as employing in his own house weavers and other workmen. He was a capitalist, with the industry under his personal control. In the sixteenth century Jack of Newbury (John Winchcombe)

had the reputation of being the greatest clothier England had yet known. He owned 200 looms within a single room. William Stumpe of Malmesbury is stated to have employed 2,000 men. The attempts to restrict cloth manufacture to corporate towns and to keep up craft prices unduly, drove the industry into the market towns and to the countryside. The clothier ceased to be a direct manufacturer and tended to become a middleman, who bought the cloth from the small country weavers and disposed of it. To do this he required greater financial resources than had hitherto been necessary. His operations were limited, not by the size of his factories, but by his cash resources. He is the forbear of the modern financier.

The corporate towns did not submit without a struggle, but in the end artificial exclusiveness yielded to economic forces. Norwich declined in the early part of the sixteenth century. It sank from second to sixth city in the kingdom. Contemporary records* show similar declines in other woollen towns and prosperity in non-corporate towns and villages.† During the reigns of Edward VI. and Mary several Acts were passed to protect the corporate towns, but, though they retarded the decline, they could not arrest it entirely. Alva's persecutions in the Netherlands had more effect.

* Leland's *Itinerary*.

† Lipson, p. 440.

From 1564 onward they drove to this country Dutch, Flemish, and Walloon cloth-workers, whose skill was greater than that of the native workers. Their arrival unsettled the cloth industry for a time. Norwich seized upon the opportunity to restore its shattered fortunes, and obtained permission for some of the immigrants to settle there. In a short time the town's prosperity was restored and its revenue doubled. Colchester enjoyed similar good fortune. On the whole, however, the corporate towns lost their privileged position, and a new type of town came into prominence. This is particularly noticeable in the West Riding of Yorkshire. York and Beverley declined, while Wakefield, Bradford, Halifax, and Leeds flourished.

In London the greater volume of commerce gave a somewhat different aspect to the economic development than in the corporate towns. In the latter the craft gild maintained its hold until threatened by the successful competition of the market town and the country-side. In London greater specialisation took place in the craft gild itself, and gave birth to the powerful livery companies. The livery was at first a sign of fraternity. Later it became the sign of wealth and exclusiveness. Those of the craft who could afford to wear the livery associated themselves to acquire power and to exclude the poorer members. They then fol-

lowed the custom of the times, and sheltered their privileges behind Royal Charters. The Taylors Company (later known as the Merchant Taylors) first came into evidence in 1267, but only obtained its Charter in 1326. The Grocers followed in 1345, and the Mercers in 1347. Later still the Vintners, Drapers, Fishmongers, Goldsmiths, Skinners, Haberdashers, Salters, Ironmongers, and Cloth-workers obtained similar privileges. The members of these companies usurped the place of the old craftsmasters. They hired the journeymen to work for them for a wage, and established the permanent wage-earning class. The journeymen's prospects of setting up as masters dwindled, though it was still open to the more successful to do so.

It is interesting to form a parallel between the infiltration of the cash nexus into the social organism as a whole and into the more limited organism of craft industry. We have seen, in the former case, the original dues in service and in kind give place to cash payments, and so bring into existence the industrial groups of the crafts. In craft industry itself the relation between master and apprentice remained for a long time largely on a non-cash basis. The apprentice gave his labour, and in return received instruction, food, and lodging. The earlier journeymen continued to lodge with the masters, receiving only a small wage until they

could establish themselves in trade. As the period of journeymanship lengthened, and journeymen took to marriage before they were established independently, they lived away from their master's house, and the food and lodging was commuted into a higher wage. The advent of the clothier and the livery companies accelerated the process until the wage basis superseded the service basis.

The livery companies were not long secure in their privileges, and soon began to feel pressure from a new source. The aggregation of cash resources, the expansion of trade, the greater enterprise of the people, led to the growth of international trade. Formerly this had been largely in the hands of foreigners, but now English merchants established connections abroad. These merchants appear to have been very largely self-made men, and, as such, were eyed askance by a writer of the sixteenth century, who complained that "the breeding of so many merchants in London, risen out of poor men's sons, hath been a marvellous destruction to the whole realm."*

As they grew in prosperity and influence, the oversea merchants followed the customary procedure of association and incorporation. They had to meet the opposition of the clothiers and the livery companies, but in the end they gained the coveted

* Lipson, p. 385.

position. The London Company of Merchant Adventurers was incorporated in 1407, and similar companies were formed in the provinces. A century and a half later the still greater aggregation of cash resources and the stimulus of maritime adventure was destined to bring into existence the great incorporated trading companies, such as the Levant (1581) and the East India Company (1600).

The fluidity imparted by the cash nexus, which slowly but surely was breaking down artificial and traditional restrictions in industry, was necessarily yet slower in its operation in the basic occupation of agriculture, partly because tradition and custom were more deeply seated, partly because the less conservative type was being lured into industry, and partly because the inherent characteristics of agriculture lend themselves less to rapid change. Such a change was, however, manifesting itself. The open-field system of cultivation was essentially non-progressive. The individual's holding was scattered in strips among the holding of the rest of the tenants. It profited little to root out weeds when they could spread again from an adjoining strip. The interlocking of services was a distinct handicap. The tenant with progressive ideas was tied both as to his time and his methods by the hidebound custom of his co-tenants. The growth of commutation gave him a slowly widening avenue

of freedom. He redeemed his control over his own time by a small money payment. The sale of his produce in the market towns increased his cash resources. He could buy out the holdings of his backward neighbour. He could consolidate several adjoining strips into a workable plot, which he could hedge round. Hence arose the fields that are a characteristic of modern England. His capacity for improvement was limited, it is true. Usually the lord was anxious for commutation, but the tenant's means were limited. One great factor suddenly came to his aid. The Black Death (1348–49) depopulated the country-side. It destroyed almost one-half of the population. In doing so, it doubled the cash resources of the remainder. Commutation fees naturally tended to adjust themselves to the altered value of money, but were slow in doing so.

The experience of 1914–20 has shown us that an alteration in the value of money will reflect itself in wages and prices of commodities sooner than in the rate paid for services. Doctors', lawyers', school fees are controlled by social custom as well as by competition. Similar influences prevailed with regard to commutation fees. The peasants could obtain enhanced prices for their produce in the towns, and could purchase their freedom. If it were denied, they could leave their holdings and go elsewhere to work as agricultural labourers. The

wages of the latter class rose rapidly. The feudal lords were in a quandary; either they had to allow commutation at the old rates or risk losing their tenants. They yielded to the needs of their situation. Later on they invoked the aid of the law, and by unworthy artifices tried to cancel the commutations. This led to the celebrated Peasants' Revolt of 1381, when the peasants avenged themselves upon the lawyers for conniving at the malpractices of the feudal lords. Economically the peasants won. In spite of reactionary legislation which followed the suppression of the rebellion, villeinage had received the fatal blow. The landlords dared not demand services from their tenants. The growth of enclosed cultivation was accelerated. The next century was to see a trend towards sheep-rearing which temporarily dispensed with the services of the labourer and depopulated the countryside. It caused stagnation in agriculture for some centuries, but brought recompense in the development of rural weaving. Service and labour dues were not destined to disappear entirely in certain localities until a much later date, but on the whole the cash nexus had prevailed.

One aspect of the transition still remains to be examined. We have traced the aggregation of cash resources in the hands of the crafts, the merchants, and the peasants. The greatest aggregation

was, however, to be found elsewhere. It has been pointed out previously that the commutation proceeded chiefly from the needs of the kings and the feudal lords to maintain troops. Sombart has pointed out the difficulty of accounting for the growth of large cash masses through trade alone. He traces it rather to the commissariat arrangements necessary for the conduct of wars and crusades. There is more than plausibility in the suggestion. It accounts for the emergence of the financier abroad at an earlier date than in England. The financiers of the early English kings were the Jews. Despite the hostility of the people, they succeeded in carrying on their business. This was possible only by enjoyment of the Royal favour. In 1290, however, Edward I. expelled them. We can be certain that this far-sighted monarch did not take such a step until he found he could dispense with their aid. Their place was taken by the financiers of Italy. Loans were obtained from Lucca (1276-92), and Florence (1294). The corporate English towns on a smaller scale also became money-lenders to the king. In 1318 Edward II. borrowed from London, and in 1351 Edward III. raised a small loan from Hereford. That the usual recourse to forced taxation was not made in these cases shows that the towns were now powerful enough to withstand royal extortion.

In 1345 Edward III. repudiated a large loan owing to Florence, and thereby caused a collapse of the Florentine banks. After that, recourse was had to Netherland financiers, and it is not until after 1400 that cash aggregations in England had become sufficiently large to enable the kings to rely upon their own subjects for their needs.

Having followed the action of the drama in this great transition from one form of society to another, let us view the technique by which it was wrought. Coins existed in England since the visit of Pytheas, a Greek, 330 B.C. Before the Roman conquest British kings issued their own coinage, with, peculiarly enough, the inscription in Latin, as, *e.g.*, "Cunobelinos Rex." During the Roman occupation commerce prospered and Roman coinage was introduced. After the Romans left the island (A.D. 400) trade disappeared and the nation relapsed. In the seventh century, however, the kings of the Heptarchy issued their own coins. Those of the kingdoms of Kent, Essex, and Mercia are known. In the eighth century the Norsemen settled in Scotland and Ireland and brought their coinage into use.* Later on, indeed, it was to be through Scandinavia that the East sent to us the silver that formed the basis of our currency. In the time of Canute money had become customary to such an

* Lipson, p. 445.

extent that heriots, the dues payable on succession to land and usually consisting of the best animals or similar payment in kind, had to some extent become commuted to a money due. In the tenth century coin must have been still more familiar, as in A.D. 991 a money tax, the Danegeld, was instituted to buy out the Danes. After the Norman conquest the silver penny was the basic coin. In the reign of the Conqueror (1066–87) the silver penny weighed 22 grains troy. It steadily depreciated in weight, a depreciation which is held to have kept it fairly constant in value, as the price of commodities was falling. In the reign of Edward III. (1327–77) it weighed only 18 grains. In that of Edward IV. (1461–83), 12 grains. Mary (1553–58) reduced it still further to 8 grains, and Elizabeth in 1601 to $7\frac{3}{4}$ grains. This constant loss of weight is attributed to the practice of the money-changers in selecting the heavier coins for export. The halfpenny and farthing were not coined until after 1200. Previously the needs for smaller change were met by dividing the penny into halves and quarters, an operation which was to find an interesting counterpart in Scotland six centuries later, when during the suspension of specie payment by the Government (1797–1823), the need for small change was met by tearing the £1 note in halves and quarters.*

* See p. 236, note.

Coinage was minted in every borough in the tenth century.* The difficulty of securing uniformity was a real one. Henry I. (1100–35) had the right hand of all the moneyers in the kingdom cut off for debasing their issues. In 1300 an Act was passed to standardise the issue by insisting upon the "London touch"—*i.e.*, that all coins should be of the standard of those coined in London. Foreign trade brought into the kingdom a varying assortment of Continental coinage, and the trade of money-changer was an important one. Gold came into use but slowly. Henry III. (1216–72) introduced gold coinage imitated from the French and Italians, but the experiment was premature. Edward III. repeated it with greater success by coining the gold noble. The pound sterling itself shows a foreign influence, the word sterling being a corruption of easterling, the name applied to the foreigners from the Hanse towns. Gold and silver issued by the Royal Mints were equally the legal tender until 1670, when silver only was made legal tender till 1717, though no ratio was fixed between the two metals. From 1717 to 1816 gold and silver were again nominally legal tender at one guinea = twenty-one shillings, but in

* Lipson, p. 176: "In the tenth century every borough was allowed at least one mint, and a larger number was accorded to those distinguished by their wealth and importance. London had eight moneyers and Winchester six; at Canterbury four belonged to the King, two to the Archbishop, and one to the Abbot."

actual practice the gold coin was the real standard one, and this practice was legalised by the 1816 Act which made silver legal tender up to forty shillings.

The coinage was at first very crude, the impression being made by a blow from a hammer. Such coins easily lent themselves to clipping, sweating, and filing. It was only at a comparatively late date (1663) that the mill and press were introduced at the Mint.

It appears remarkable that such a slender mechanism should have been the agent in breaking up one form of society and fostering another. Yet cash money acted as a solvent upon the rigid feudal organism, slowly dissolving its crust and setting free industrial layers which in turn tended to crystallise out. The solvent, however, penetrated still deeper and set free fresh layers, so that the partially crystallised layers broke down under pressure from above and below, until the whole of the organism promised to become fluid and each molecule in it endowed with equal freedom of movement. That process was not to be completed. The organism was later to develop symptoms of increasing rigidity. The differentiation between the classes was to become once more increasingly definite until modern society is threatened with a return to the primeval caste system. The study of this process will, however, take us out of the time of the cash nexus into the modern era of financialism.

Chapter Four: *From Cash Nexus to Credit Restriction*

It is a long journey from the Middle Ages to the time when a group of powerful financiers is destined to throw the sinister shadow of an unseen despotism across the world.* Let us trace in this chapter the first stage of historical development, a stage so fraught with industrial progress that the latter part of it has aptly been termed "the industrial revolution." Its financial aspect is characterised by the conflict between the powerful and privileged Bank of England and the small "six-partner" banks, ending in the extinction of the latter.

In the earlier days of finance its centre was in Italy and the Netherlands. The Bank of Venice was founded about 1400, that of Genoa 1407, Amsterdam in 1609, then followed Hamburg and Rotterdam. The Bank of England was not founded until 1694, at a time when English enterprise was

* President Wilson, p. 145: "The great monopoly in this country is the monopoly of big credits. So long as that exists our old variety and freedom and individual energy of development are out of the question. A great industrial nation is controlled by its system of credit. Our system of credit is concentrated. . . This is the greatest question of all, and to this statesmen must address themselves with an earnest determination to serve the long future and the true destinies of men."

already making itself felt over the known world. The world's financial centre quickly passed from the Continent to England. The pride of place remained unchallenged until recently, when a re-grouping of financial interests round New York has given serious cause for reflection. In studying English banking we are indirectly studying that of the world. All countries have conformed more or less to the English system, and the effects of that system are to be felt throughout the world's industrial organism.

The genesis of banking was in the craft of the goldsmiths. We have already seen that the variety of foreign coin in England had rendered the trade of money-changer an important one. The money-changer merged into the goldsmith. In the fifteenth century the English goldsmith could compare favourably with his fellow in other countries. A Venetian, writing at the end of the fifteenth century, stated: "In one single street, named the Strand, leading to St. Paul's, there are fifty-two goldsmiths' shops, so rich and full of silver vessels, great and small, that in all the shops in Milan, Rome, Venice, and Florence put together, I do not think there would be found so many of the magnificence that are to be seen in London."

The aggregation of cash resources in the hands of the London merchants has been mentioned in the

last chapter. The need for some safe place for storing money until it should be required for commerce made itself felt. The natural place to suggest itself was the city's stronghold, the Tower of London. But the merchants reckoned not upon the perfidy of princes. In 1640 Charles I. seized £130,000 of merchants' deposits. True he restored it, using it as a lever for a forced loan of £40,000, but the merchants had learnt their lesson. They preferred to keep their treasures in their own possession or in charge of their cashiers. Here again, however, there were pitfalls. During the Civil War which shortly ensued (1642) cashiers shared the prevailing custom of going to fight with the armies, and were not always averse to taking some of their master's treasures with them. The merchants found they could trust their cashiers as little as their king. The only class that inspired sufficient confidence was the goldsmiths, and the practice developed of depositing money with them.

To this practice is traceable the origin of both the cheque and the bank-note. The merchant, when he had large payments to make, would at first withdraw his money. Later on he hit upon the expedient of giving an order upon the goldsmiths to pay over the sum to the creditor. The economy in the case where both debtor and creditor deposited with the same goldsmith is obvious. The merchant's

order upon the goldsmiths to pay is the origin of the modern cheque. The goldsmiths gave receipts for all deposits placed with them, and soon the goldsmiths' receipts were used instead of merchants' orders to pay. Their circulating power was better. The goldsmiths were trusted, and their notes were freely accepted. They were the foundation of the modern bank-note. Nor was their popularity short-lived. Even after the foundation of the Bank of England they were in common use.* The triumph of the goldsmith's note over the merchant's order to pay was a purely economic one. It supplies a historical corrective to the modern view that the cheque has supplanted the bank-note because it is a better instrument, the truth being that the cheque only survives because the issue of notes has been everywhere restricted.

During Cromwell's protectorate (1649–60) there was perfect security in the land. The Jews were allowed to return, though the legislation against them was not specifically withdrawn. The goldsmiths prospered exceedingly and the people trusted them. They began to be referred to as bankers. In the reign of Charles II. (1660–85) their lot was not so happy. Charles II. was a spendthrift; he

* Davenant, *Discourses on the Public Revenues and Trade of England*, vol. ii., p. 161: "All great dealings were transacted by tallies, bank-bills, and goldsmiths' notes."

kept a standing army and a large fleet. He indulged in inconclusive wars with the Dutch. All this cost money. Charles got as much as he could from his good cousin, Louis XIV. of France, and when that proved insufficient he borrowed. Naturally enough he borrowed from the wealthy goldsmiths. Having done so, he took the shortest way out of the difficulty, that of refusing to pay back. In 1672 he suspended payment out of the Exchequer for twelve months. At that time he owed the goldsmiths £1,300,000, which represented the deposits of the merchants. Some ten thousand persons were ruined by this gracious princely act. Later he promised to repay, but negotiations were protracted, and it was only in 1705, in the reign of William and Mary, that the goldsmiths began to recover a small portion of the debt. Charles's action helped to settle the fate of the Stuart dynasty. It alienated the merchants. Charles indeed lived and died a king, but his brother James had a short reign of three years, when the country dismissed him and called William of Orange to the throne. William responded to the call, and became king of England in 1688. He saw the need of binding the commercial interest to his cause. The goldsmiths' prestige had suffered a blow by the acts of the Stuarts, but the need for banking facilities was urgent. In 1694 the Bank of England was founded.

The commonly accepted view of the Bank of England is that it is a paternal institution carefully watching over the financial good of the people and using its monopoly for their welfare. This view is unhistorical. The Bank of England was from its inception a privileged monopoly, jealous of its supposed rights as all monopolies are, short-sighted and deaf to the demands of progress. Its monopoly in the first case consisted in the fact that it was the sole bank to obtain an Act authorising its foundation. When in 1696 the king promoted the foundation of the Land Bank, the Bank of England seriously set to work to protect itself. The Land Bank was a fiasco. It was formed on an absurd principle, that money could be lent on land to a greater amount than the land was worth. Only £7,100 was subscribed to the issue, of which the king contributed £5,000.

The Bank of England was founded with financial resources of £1,200,000, individual subscriptions being limited to £20,000. The entire sum was lent to the Government at 8 per cent. interest, plus a charge of £4,000 for management of the debt. The Bank therefore had an income of £100,000, but no cash resources save what it could obtain from deposits. The notes it issued bore interest at the rate of 2d. per diem per £100 (= 3 per cent.). This practice ceased in 1709. The convertibility of these notes in the earlier days could only be

secured by the directors themselves finding the cash for redemption when necessary. The failure of the Land Bank was used as a lever by the directors to increase their capital by another £1,001,171, and to obtain a real monopoly by the legislative provision that no other corporation in the nature of a bank should be established by Act of Parliament. The Bank of England was allowed to increase its note issue from the original £1,200,000 to the amount of its subscribed capital, but the notes must be payable on demand. This precluded the use of the "option" clause, which was to play such an important part in Scotch banking later on.*

The provision against the formation of other banks under Act of Parliament did not shield the Bank of England from competition. The Company of Mine Adventurers, a fraudulent creation, constituted itself a note-issuing bank. Once more the Bank of England stirred itself in the defence of its monopoly. The Act of 1709 made it unlawful "for any body politic or any corporation whatsoever united or to be united in covenants or partnerships exceeding the number of six persons, in that part of Great Britain called England, to borrow, owe or take up any sum or sums of money on their bills or notes payable on demand or at any less time than six months." A similar restriction was subsequently

* See Chapter IX.

to be made in Ireland, within a radius of sixty-five miles from Dublin, in favour of the Bank of Ireland, but fortunately Scotland never suffered from this form of legal tyranny.

The "six-partner" restriction obtained for over a century, during a period which was to inaugurate the greatest industrial revolution the world has ever known. It is of the utmost importance to bear this in mind in considering the failure of the industrial revolution to realise the hopes which it called into being. Even in 1826, when the Bank of England consented to abandon this form of monopoly, it only did so in favour of an equally vicious one, that no bank of issue should be founded within sixty-five miles of London. With assured control of the world's financial centre it could eye with equanimity the competition of its provincial rivals.

The first Bank of England notes issued were for large amounts, not less than £20. They were secured, be it observed, not upon tangible assets, but upon debt, the debt due by the Government to the Bank. The security of one form of paper upon another form of paper would appear to common sense somewhat illusory, and has been violently challenged. MacLeod says:* "Each loan to Government was attended with an *augmentation* of currency

* MacLeod, *Theory and Practice of Banking*, sixth edition, vol. i., pp. 487-488.

to an equal amount. Now to a certain extent this plan might be attended with no evil consequences, but it is perfectly clear that its *principle* is utterly vicious. There is nothing so wild or absurd in John Law's Theory of Money as this. His scheme of basing a paper currency upon land is sober sense compared to it. If for every debt the Government incurs, an equal amount of money is to be created, why here we have a philosopher's stone at once. What is the long-sought El Dorado compared to this? Even there the gold required to be picked up and fashioned into coin."

"Granting that to a small extent this may be done without any practical mischief, yet, as a general principle, what can be more palpably absurd?"

MacLeod's question has gone unanswered. Its legacy remains for the present generation. Neither Governments nor Government-controlled banks have mended their ways. The Bank of France has notes in circulation to the amount of francs 37,100,000,000 secured as to francs 24,900,000,000 on advances to the State. England has a Treasury note issue of over £M300* secured only as to £M28½ in gold, £M19½ in Bank of England notes, and the rest representing Government debt.† The

* £M signifies million £ throughout this book.

† September, 1921.

practical mischief is being done. The currency has depreciated with respect to almost the only convertible gold currency left, that of the American dollar. Upon the ability of the nations to redeem their huge debts is staked the economic prosperity or disaster of their peoples.

Let us trace the onward sweep of the industrial revolution. In 1698 Savery invented his primitive engine for clearing water from mines, showing that deep mining was already in hand. In 1705 Newcomen improved upon Savery's invention. In 1709 ironworks were founded at Coalbrookdale. In 1719 silk spinning was introduced by Sir Thomas Lombe. In 1733 Kay's flying shuttle increased the rate of weaving. These were but some of the forerunners of the still greater volume of industrial expansion in the latter half of the century.

The cash nexus had proved insufficient for the needs of industry. The additional aid of the Bank of England note could not satisfy the demands for currency. Banks commenced to spring up in the provinces. Small tottering institutions they were, doomed to inadequate resources by the "six-partner" restriction. Still, they were all that could be had, and with their help England struggled forward. In 1750 twelve such banks had already been founded, each with its own note issue. In 1750 also, James Watt experimented with the power

of steam. In 1755 ironworks were started at Merthyr Tydvil. In 1759 the Bank of England supplemented the unwieldy £20 note by £15 and £10 notes.

The year 1600 had seen the formation of the first joint-stock company, the East India Company. Previous companies were simply merchant gilds incorporated to exploit a territorial monopoly, but with no joint liability. The growth of joint-stock companies was a characteristic of the seventeenth century. New lands were everywhere coming into the economic ken. Speculation in such ventures grew warmer and warmer, and finally boiled over in the great South Sea Bubble (1720). That episode is too well known to need description. The Bank of England had a narrow escape.* Parliament passed the Bubble Act to regulate the increase of joint-stock companies. The largest commercial enterprises, however, now involved such cash requirements that individuals could rarely undertake them. Hence Parliament had to sanction the incorporation of joint stock companies to an increasing extent. The dealing in shares of such companies became a separate branch of industry, and in 1759 the London Stock Exchange was founded.

* Andréadès, p. 145: "It (the Bank) escaped the second and later danger which resulted from the failure of the South Sea Company only by breaking its word, and it only withstood the run upon it by using methods unworthy of a great establishment."

Meanwhile the cotton industry was slowly progressing. In 1760 the export of cotton was only twentieth that of the woollen industry. But the former industry had one great advantage. The woollen industry was choked with Government regulations. Its younger rival's freedom of development was comparatively untrammelled. In 1764 Hargreaves invented the spinning jenny, in 1769 Arkwright the water frame, in 1779 Crompton the mule, in 1785 Cartwright the power loom. Lancaster began to prosper. It attracted men of enterprise. Brindley, that untaught genius, built his first canal in 1761 between Worsley and Manchester; he followed this up, in 1766, with the one between Manchester and Liverpool. Soon his celebrated navigators, or "navvies", were at work over England. Watt in 1769 patented his steam-engine. England was forging ahead. The growth of national wealth attracted the attention of the social student. In 1776 Adam Smith wrote his *Wealth of Nations*.

What was the Bank of England doing to promote the growing industry? It was keeping at least one eye upon its monopoly.* It obtained a renewal

* Andréadès, p. 171: "The Bank of England, playing in this matter the part of dog in the manger, not only did not found branches to issue notes, but was unwilling to allow powerful and well-established companies to be formed for the purpose. . . . The consequence was that wealthy and respectable companies

of its charter in 1742 by an Act which reiterated the "six-partner" restriction for all other banks. In 1764 it paid £110,000 for another renewal. In 1781 it lent £M2 to the Government for a further extension, and in 1800 £M3 in a similar bargain. It patriotically came forward to assist the Government in its wars, but economic history is silent as to its endeavours to help industry.

The community turned for financial support to those flimsy partnerships of 6 persons which the law allowed. Their number increased enormously. From 12 in 1750 they had risen in 1795 to no less than 400, and in 1810 to 721.* Simple arithmetic will show that the whole financial transactions of the nation, apart from the Bank of England, rested upon the shoulders of less than 4,400 persons. Hastily springing up in response to an urgent need, many of these small partnerships lacked both financial and business stability and perished almost as soon as formed. Others rose in their stead. Some of their directors were unscrupulous, some were incompetent, some lacked substance. In

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were unable to issue notes, and that, since the country needed a circulating medium and could not get a good one, it was soon supplied with a bad one. A number of shopkeepers, chemists, tailors, and bakers, taking advantage of the clause authorising banks formed by less than six persons, became bankers and flooded the country with worthless paper."

* Powell, p. 118.

those cases the banks failed. Sudden and uncalled-for runs could be stopped by the use of the "option clause" or "post-dated" note, which steadily increased in use, but this safeguard was forbidden in 1765. More democratic than the Bank of England, the provincial banks abandoned the high value notes for notes of small amounts, in accordance with the pressing needs of the time. Undoubtedly they overdid it, but they were feeling their way in the midst of financial obscurity. The paternal State, knowing the needs of commerce better than commerce itself, prohibited notes of less than £1 in England in 1775, and improved upon this in 1777 by increasing the minimum value to £5. During the currency restriction period of 1797–1823 small notes were again allowed, but were a second time prohibited.

It is a significant fact that the main industrial revolution was accomplished outside London. No great invention or enterprise appears to have had its birth in the metropolitan city. The Bank of England did not deliberately choke progress, but it lacked the incentive to enterprise that free competition alone can give. The area of its commerce is not clearly indicated, but it is a fair assumption, from the fact that in 1826 the Bank of England suffered the "six-partnership" restriction to be withdrawn in favour of a monopoly of note issue

within sixty-five miles of the capital, that that radius was the extent of its effective influence. No small upstart private bank could compete at too close a range with the powerful corporation. The better known of the private banks, at any rate, were further afield. The area within the sixty-five miles radius became industrially the least developed in England. The home counties dropped back into the agricultural stage. The metropolis itself sank from a city of industry to one of merchants and middlemen. It now lives on largely as a parasitic growth upon the industry of the rest of the country.

In the Middle Ages London and the towns near it had their industries. Spitalfields had its silk trade; Guildford was known in the fourteenth century for its cloth. The Weald of Sussex had its ironworks: in 1740 there were still ten furnaces at work, with an output of 1,400 tons per annum, but the industry was already a declining one.* Yet the other agricultural counties in England prospered under their provincial banks. Defoe, in his *Tour*, tells of the cloth industry of Bradford in Wiltshire and of Frome, the serge of Devizes, the dyed cloths of Stroud, the industries of Trowbridge and Taunton. That belt of country, fifty miles by twenty, from Cirencester in the north to Sherborne in the south, from Witney in the east

* Toynbee, p. 49.

to Bristol in the west, was, according to him, "a rich enclosed country, full of rivers and towns, and infinitely populous, insomuch that some of the market towns are equal to cities in bigness and superior to many in number of people."*

This flourishing district included, in addition to its rivers, other assets, such as Wood's Bank in Gloucester, founded 1716, originally a candle shop, the Bristol Old Bank (1750), Gillet's Bank at Witney, Stuckey's Bank in Somerset. Lincolnshire possessed Smith's Bank at Lincoln, and Garfit's Bank at Boston, and its agricultural machinery might claim with some right to be the best in the world. "By 1800," Toynbee says, "the manufacture of silk hosiery had centred in Derby, that of woollen hosiery in Leicester, though Nottingham had not yet absorbed the cotton hosiery. But at the beginning of the century there were still many looms round London and in other parts of the South of England. In 1750 London had 1,000 frames, Surrey 350."†

In 1779 the first iron bridge was constructed at Coalbrookdale. In 1783 Bell introduced calico printing. In 1785 Watt's engine was applied at Popplewick in Nottinghamshire to cotton mills. In 1790 the first iron vessel was built. In the same year Symington made his first attempt with the steam

* Defoe's *Tour*, seventh edition. † Toynbee, p. 50.

tug, and was successful some twelve years later. Wakened out of the torpor of controlling regulation by the strides of the cotton industry, the woollen manufacturers bestirred themselves. In 1800 they adapted cotton machinery to their own business. In 1808 Heathcoat produced his lace-making machine, and in 1813 Blackett's "Puffing Billy" marked another step in progress, while in the same year Bell's *Comet* appeared on the Clyde. Stephenson was heard of in 1814. Pit-props were first used in 1795, and the invention of the Davy lamp (1815) shows that mining was reaching deeper levels, where explosive gases were to be met with. In 1814 the first woollen mill was established at Stanningley near Leeds, the event marking the decline of weaving at home. Roads underwent improvement, Macadam introducing his system in 1815. In 1825 the first railway was laid between Stockton and Darlington, to be followed in 1830 by that between Liverpool and Manchester.

The rise of industry was accompanied by an advance in agriculture. The common field system had lingered on. Enclosures had been made sporadically in the previous centuries, but in 1750 the old communal method of husbandry still checked progress over the greater portion of the arable land. According to Toynbee, "though these common fields contained the best soil in the kingdom,

they exhibited the most wretched cultivation."* Arthur Young states: "Never were more miserable crops seen than all the spring ones in the common fields, absolutely beneath contempt."† The trend toward enclosed cultivation was noticeable in Norfolk in the first half of the eighteenth century. The enclosures were economic in origin and made without Parliamentary aid. The result was that Norfolk developed an improved type of husbandry, which made the name of this county so famous in the farming world.‡ Stock-breeding attracted attention. From 1760 to 1785 Bakewell reared his celebrated "Leicester" breed of sheep. At the same time the brothers Culley produced the Shorthorn or Durham breed of cattle. Tull's system of husbandry, which he practised in Berkshire in 1701, died with him, and was not revived again until shortly before 1770. The supremacy of enclosed lands over common fields became so obvious that from 1774 onwards Bills were introduced into Parliament to enforce enclosure.§ The first General Enclosure Act was passed in 1801, and others followed.

* Toynbee, p. 39.

† Young, *Southern Tour*, p. 354.

‡ Young, *Eastern Tour*, p. 150.

§ M. Beer, *A History of British Socialism*, vol. i., p. 96: "The economic superiority of enclosed or private agriculture over the open field or communal agriculture was so striking that nobody denied it."

But legislation accomplished with great injustice what the economic trend had effected smoothly elsewhere. The labourers were dispossessed with scant regard to their rights, and bitter indignation was aroused.

The action of the private banks in the promotion of agriculture is worthy of notice. The anonymous author of *The Utility of Country Banks Considered*, writing in 1802, and speaking of the Gainsborough district, says: "Sandy heaths and marshy bogs have been converted into fertile fields, and several extensive enclosures have been undertaken, to the great advantage of the country and the profit of individuals, which improvements have been greatly promoted by the banks of that thriving town."* Again he narrates: "I had an opportunity of observing the improvements which have taken place within a very few years in one of the most barren and desolate parts of England, I mean the Wolds of Yorkshire, whose bleak mountains, which hardly furnished a blade of grass to a few famished sheep, are now waving fields of corn. The crops of oats and barley were, this last harvest, immense. . . . Improvements like these are objects of national importance, and it is my opinion that they never could have been effected without the aid derived

* Pamphlet published by J. Hatchard (see Jevons' *Collection of Pamphlets*, vol. xlix., p. 54).

from the country banks. The Bank of England would not have advanced the sums necessary."*

Let us turn for a moment from these glorious triumphs of economic history, won by enterprise and competitive banking, to international relations. France had been under a powerfully centralised monarchy. Militarily it had had a period of glory. Louis le Grand Soleil gained victories by his marshals over all his enemies, but towards the end of his reign the tide turned, and when his sun set he left an impoverished and hungry people. Economically they were still in the stage of craft industry. The two succeeding reigns saw matters go from bad to worse. The royal expenses grew while the people became poorer. In 1789 the great Revolution broke out. How hateful craft restrictions must have become is shown by the fact that one of the earliest acts of the Revolution was to abolish the gilds (1791). The rise of Napoleon is not essentially a matter of economic interest, but his war with England was fated vitally to affect the world's financial future. He had to fight the world's great financial power, and he fought it with the same weapon. He had no State Bank when the conflict began, but he soon learnt the need for it. Doubtless he found that private banks preferred the innocent

* Pamphlet published by J. Hatchard (see Jevons' *Collection of Pamphlets*, vol. xlix., p. 72).

gains of commerce to the destructive profits of war. In 1800 he established the Bank of France. In 1803 he bestowed upon it the privilege of note issue in Paris and other cities where it had branches. In 1848 it acquired an exclusive privilege in this respect.

The war between England and France was waged between an industrial country and a military genius. England won rather by its factories than by the small but dauntless armies that it despatched to fight the Corsican.* The Continental nations were vanquished with surprising ease, but England supplied the sinews of war for them to fight again. The man-power of France was sapped by years of campaign while the industrial resources of England grew.

From the financial point of view, the war was one between two States supported by their privileged banks up to the pitch of almost ruining their respective nations. The position in England was that there was one bank only with ample cash resources, the other 400 being stunted in this respect by an absurd restriction. Such scanty cash resources as they could command were drained from them, not

* Lecky, p. 218: "The first and most obvious fact is that the triumphant issue of the great French War was largely, if not mainly, due to the cotton-mill and the steam-engine. England might well place the statues of Watt and Arkwright by the side of those of Wellington and Nelson."

for the arts of peace, but for the devilries of war. The Government began to call upon the country's cash resources. In 1793 a loan of £M6¼ was issued. Between 1793 and 1801 loans to £M314½ were issued, of which £202,372,000 was raised. The withdrawal of cash resources was a hard blow to the country banks. The weakest went to the wall. In November, 1793, in one month alone, out of the 400 banks, 100 failed, while 200 others were severely shaken. The drain of gold was first felt at Newcastle, where the banks stopped payment. The shareholders had adequate resources to meet all demands upon them,* but the Government had filched their gold and denied them the protection of the "option" clause or post-dated note.

The internal strain upon gold was followed by an external one. In 1795 England made its first foreign loan to Germany, £4,600,000; in 1797, a second one of £1,620,000. Up to 1801 £M15 was raised for the benefit of our Allies, of which more than £M9 was paid in cash. Again the provincial banks succumbed to the withdrawal of their cash resources. The crisis of 1797 originated, according to both Baring and Tooke, in the latter half of 1795.† In 1793 nearly £M3 was exported

* Andréadès, p. 188.

† Sir Francis Baring, *Observations of the Establishment of the Bank of England*, London, 1797, pp. 178-179; Tooke, Thomas, *An Enquiry into the Currency Principle*, London, 1844, pp. 192-211.

in cash for loans and other purposes, in 1794 £M8, in 1795 £M11. Even the Bank of England with its larger resources found it necessary to protest emphatically. In December, 1794, it declared it could no longer assist the Treasury. Pitt replied by obtaining a fresh advance of £M2.

Again the crisis began at Newcastle, the concentric drain of gold towards London naturally making itself first felt at the most distant point. The panic swept through the country, and threatened to destroy the Bank of England itself. The latter's cash resources dropped to £1,272,000. There was no alternative but to suspend cash payments. On May 3, 1797, the Bank Restriction Act was passed, forbidding the Bank to make any payments in cash to any creditors or to use cash for any payments except to the Army and Navy or in pursuance of an order from the Privy Council. This Act remained in force till 1823.

The industry of the country was threatened with ruin. The country banks had to restrict and call in their advances, and their clients were obliged to cover themselves by forced sales of securities, factories, and goods at immense sacrifices.

To what was the disaster due? To the instability of the provincial banks, says the complacent school of orthodox economy. Not at all. To the shortsightedness of Government. The war may have been

a historical necessity, but Government restrictions had prevented a financial system being established on sufficiently strong foundation to stand the shock. The privileged Bank of England supinely handed over the nation's cash resources for export to Continental Allies, and industry received the worst set-back it had known since the inauguration of the industrial revolution.*

The country banks never recovered their prestige. Staunch supporters they found in plenty to plead their cause, but the trend of history was against them. Not economic history, be it remarked, but political history. Militarism was rampant, and privileged interests waxed under its shadow. With the decline of the country banks we see the beginnings of that movement of unrest among the workers which in the long run so strangely upset the philosophic tenets of the Manchester school.

The industrial revolution had not been accomplished without an immense amount of economic disturbance. The depopulation of the country-side of the first half of the fifteenth century had given place to a prosperous population, combining the

* MacLeod, vol. i., p. 533: "This disaster was the second notable penalty which the country paid within four years for the unjustifiable monopoly of the Bank. Never was there a more unfortunate example of monopolising selfishness; it would neither establish branches of its own in the country, nor would it permit any other private company of power and solidity to do so."

still primitive agricultural methods with weaving at home. The improvement in agriculture in the latter half of the eighteenth century was localised and slow in spreading. The growth of the factory system struck a blow at the country-side's method of livelihood. It displaced the domestic weaving industry. At the same time it offered to labourers good wages in the towns.* It offered the most enterprising men chances of rising on the flowing tide to the position of large employers. They gladly availed themselves of the opportunities, and flocked to the new factory centres. While the provincial banks were allowed to carry on their beneficent work, complaints were scarcely to be heard except from the agricultural labourer, whose attachment to the soil left him an industrial derelict.

When the provincial banks succumbed to the State's folly, the vista changed. No longer could factories be erected to absorb the growing army of industrial workers. Expansion did not cease at once, but it lost velocity. The stress of lessening employment and worsened prospects provoked cries of complaint from the worker, which steadily grew in volume. In 1802 the State interfered, taking the first step in regulating factory industry by protecting pauper labour. In 1831 the insistent appeals of

* The cotton industry employed 40,000 operatives in 1760, 80,000 in 1785, and 833,000 in 1831.

the humanitarians further prevailed over the Manchester theories. It was a question of fact against doctrine. Protective legislation was extended to children. In 1844 it was further extended to women. Manchesterism fought with wonderful eloquence, but Manchesterism lost. The disillusioned workers became conscious that the system was not working to their advantage. Machines assumed the guise of evil spirits to be exorcised at all costs.

Antagonism to the introduction of machinery was nothing new. The gilds had always resisted it.* Now, however, the antagonism took a violent form. In 1812 the Luddites started their machinery-breaking campaign. Industrial expansion was threatened from many sides. The vitality imparted by the provincial banks had been impaired, the credit

* Lipson, p. 426: " The introduction of machinery was inevitably a fruitful source of dissension. The shearmen objected to the use of ' instruments of iron,' and a statute of 1495 ordered fustian cloth to be shorn ' with the broad shears only.' . . . Objection was also raised (1552) against the use of the ' wrinch, rope, or ring, or any other engine ' for straining or stretching cloth. But the most persistent of all was the agitation over the use of water-mills among the fullers. Fulling at mills instead of ' by might and strength of man ' was forbidden in London as early as 1298, and again in 1376, 1391, and 1404. In 1417 the prohibition was annulled on the ground that fulling by mills involved less cost and was equally serviceable, but in 1437 it was once more revived and confirmed in 1483 by statute."

of the country was swaddled by legislation, the cash resources were sapped by foreign loans, the worker was disappointed and defiant. The country struggled on. The Napoleonic wars were finished in 1815, leaving the nation crippled and prostrate, but recovery was not long in manifesting itself. The cessation of the cash drain enabled the provincial banks to flourish again. In 1821 cash payments could be resumed, though not legally restored until 1823. Elasticity in credit developed once more. Manchesterism was at the height of its triumph. In 1823 Huskisson initiated his Free Trade policy.

The Napoleonic wars over, England returned to the financing of overseas enterprise. From 1822 to 1825 millions of pounds were invested in South American republics.* England, freed from restrictions as regards cash payments, was again prospering. Tooke states that industry and commerce were never so flourishing as between 1821 and 1824. The harvests in 1822, 1823, and 1824 were exceptionally good.† A new speculation mania took place. It was the South Sea Bubble again. Companies were founded to the number of 624, with financial resources of £M372. Then came the crash. The Bank of England's reserve cash dwindled in 1824 from £M13½ to £M11½. In April, 1825, it had

* MacLeod, vol. ii., p. 109, estimates the amount at £M150.

† Andréadès, p. 248.

sunk to £6,650,000. Who was to blame? Andréadès emphatically puts the blame on the Bank, but the Bank itself was bound by restrictive legislation. It raised its rate to 5 per cent., the limit fixed by the Usury laws. The remedy was not sufficient, its reserves sank lower and lower, and in December, 1825, were only £1,260,890. The drainage of cash resources to South America continued. Cash disappeared, though the Mint worked day and night. Stocks had to be sold at a ridiculous figure. Once more the flimsy provincial banks, with no method of protection and with their restricted cash resources, quailed before the storm. Thirty-six of them failed. The Bank of England put into circulation 600,000 £1 notes, gave new advances of £400,000, and the crisis passed.

In spite of the aid of the £1 note in the 1825 crisis, notes under £5 were again prohibited in 1826, as the growing note issues of the provincial banks excited the jealousy of the Bank of England. At the same time the need for a more stable form of provincial bank was at last recognised, and the Bank of England reluctantly allowed the withdrawal of the six-partner limit in exchange for a monopoly of all note issue within sixty-five miles of London. The legislators were even so ill-advised as to propose to extend the prohibition of notes under £5 to Scotland. They were startled at the oppo-

sition the proposal provoked.* A whole nation rose in indignation. Sir Walter Scott, the great novelist, championed the popular cause. Rebellion was in the air and the Union was in danger. The advantages or disadvantages of the small note were a matter of intellectual discussion to English statesmen. To the Scotch people, who had risen to industrial triumphs by its aid, it was a matter of vital importance. The advantage of the £1 note over the £5 was demonstrated by the inflow of Scotch notes into England, so the circulation of these was prohibited in the latter country in 1828.

The Act of 1826 allowed the formation of joint-stock banks in the provinces, with right of note issue. It did not prevent the formation of similar institutions in London without such a right. So great was the need of financial accommodation that banks at once sprung up, availing themselves, in the absence of notes, of the method of cheque payments. The Bank of England, selfish to the end, could not tolerate the competition. It used all its influence with the Government, but it lost. The matter was referred to a Committee. The Act of 1833 was the result. It made Bank of England notes legal tender, and exempted the Bank from the Usury laws in respect of bills of not more than three months,

* Kerr, p. 202: "They excited the most extraordinary criticism in Parliament and elsewhere, as calculated to foster rebellion."

a valuable lesson from the 1825 crash. It did something more in reaffirming the legality of the joint-stock banks. The effect was remarkable. In the years 1835-36, upwards of one hundred new banks sprang up in England and Wales. Among them were the London and Westminster and the London Joint-Stock Bank. In 1839 the Union Bank and the London and County Bank were founded. These joint-stock banks were those very stable institutions which the country had yearned for during a century of expansion and warfare. The slender six-partner banks handed over to them their task. All the big banks in England to-day were founded after 1833. Those founded before then have been swallowed up or crowded out. The Bank of England fought for its monopoly with an energy worthy of a better cause. The joint-stock banks, led by men like Gilbart, met power by ruse until in the end the Government was forced to intervene (1844).

The lessening of the Bank of England's monopoly by the Act of 1833 was followed by three years of great prosperity. The competition of the new joint-stock banks lowered the rate of interest. Commerce and agriculture prospered. The harvests of 1834, 1835, and 1836 were exceptionally abundant.* Foreign countries raised loans in London to the ex-

* Andréadès, p. 263.

tent of £M20. Railway, mining, canal, and banking companies were floated to the amount of £M135.

The first shock came from America. President Jackson resolved not to renew the charter of the United States National Bank. This caused a panic, and the American houses sold all sorts of securities to the English banks. The Bank of England alone advanced £M6. Then the harvest failed in 1838. England had to import cereals to the value of £M10 and export gold to do so. The Bank of Belgium failed at the end of 1838; the Bank of France protected itself by calling upon London for gold. Again the management of the Bank of England was at fault. In spite of the demands upon it, it reduced its rate of interest from 5 to 3½ per cent. in November, 1838. When the failure of the Bank of Belgium gave it an unmistakable warning it thought fit to send another £M1 to America.* In May, 1839, it realised its situation, and raised its rate of interest to 5 per cent. Its reserve had then fallen to just over £M4. In July it sank to less than £M3, and the Bank of England was faced with bankruptcy. It tried to sell securities, but there were no buyers. In desperation it had recourse to the Bank of France.

* MacLeod: "Of all acts of mismanagement in the whole history of the Bank, this is probably the most astounding" (quoted by Andréadès, p. 267).

Through the mediation of the Baring Brothers technical difficulties were overcome, and a loan of £M2 was arranged. The Bank had saved itself from its own folly, but at a cost to the community. Sixty-three other banks were dragged into failure, of which twenty-seven had separate note issues.

The crisis of 1839 profoundly agitated the public mind. England was the world's financial centre, and was without protection against demands upon its cash resources from abroad. The only protective device which had suggested itself to the bankers, the option clause or post-dated note, had been prohibited by the legislators. The interest aroused in the question is shown in the extraordinary number of pamphlets published at this period.* Gradually the conflicting theories ranged themselves round two main principles: the Banking Principle and the Currency Principle.

The chief exponent of the Banking Principle was Tooke. The principle affirmed that the note issue should be unrestricted by the State as to quantity—that the community would protect itself against over-issue. Its adherents were not averse to State control of quality—*i.e.*, protective measures against issue by worthless firms.† In this they were

* An interesting account of the War of the Pamphlets will be found in Henry Meulen's book (see Bibliography).

† Tooke, *History of Prices*, vol. iii., p. 206: "I am here assuming as an undoubted right on the part of the State the principle that banks of issue are properly subjects for regulation."

false to themselves. The obvious remedy against bad notes was by promoting the competition of sound institutions which was now coming into play as a result of the Act of 1833.

The Currency Principle was most ably represented by S. J. Loyd (afterwards Lord Overstone). His school maintained the extraordinary principle that note issue was quite a distinct function from all other banking business, and that note circulation should be forced to correspond with the variations in bullion or cash reserves.

The argument was ably conducted on both sides. The Currency Principle won. The cynic may attribute its triumph, not to superiority of argument, but to the fact that its adherents (including the Bank of England) represented a greater weight of interest than its opponents. But the Currency Principle did not score a complete triumph. The absurdity of trying to apply it in its absolute terms was too apparent. Even Lord Overstone compromised. According to him the issue of notes should be confided to a bank exclusively established for this object. "The importance of a rigid adherence to this principle cannot be over-estimated; and if it be incompatible with the mixed functions of the Bank of England, it seems to become a serious question whether it is not better to separate altogether the business of banking from that of regulating

the currency, rather than suffer so essential a rule to be in any degree compromised." The impossibility of such an act was too great even for Overstone to urge it. Torrens hit upon a compromise. Instead of having a separate bank of issue, the Bank of England was to be divided into two departments. This was a veritable judgment of Solomon. The proposal was incorporated in the Act of 1844.

The Currency Principle failed in another point. It alleged that note issue should be based upon bullion. But the country's commerce was being carried on by a note issue not entirely covered by bullion. To reduce it to the necessary amount would be to court disaster. To allow it to expand would be to allow a repetition of the 1839 panic. The solution was obvious. It must be fixed as it stood. Whatever the future needs of commerce, however great the expansion in industry, howsoever pressing the demands of finance, the uncovered note issue of the country must remain at the then level. This was also secured by the Act of 1844. The provisions were simple. The note issue of provincial banks was not to exceed the mean of the twelve weeks preceding April 27, 1844. All banks ceasing to redeem their notes on demand were to lose their right of issue. No private banks could amalgamate and issue notes if the amalgamation resulted in an association of more than six persons.

The notes of private banks were not to be legal tender.

The intention of the Act was to eliminate the private issues. It has succeeded. When it was passed there were 207 private banks and 72 joint-stock banks of issue in England, with a circulation of £8,631,647. They have all disappeared.* The note issue has been transferred to the Bank of England.

The Bank Charter Act of 1844 was the crowning piece of financial legislation. Every other nation has copied it. True, none have accepted it in all its rigidity. The Federal Banks of America and the Reichs-bank of Germany have a greater degree of flexibility, which has been an important factor in enabling these nations to overtake their rival. In the main, however, the views of Overstone and Torrens have prevailed. From 1844 onward we have to face the melancholy spectacle of economic society gradually losing its fluidity. Rigidity becomes increasingly pronounced in the social organism. The working masses are born to a life of toil from which there is no reasonable prospect of escape. At the other end arises a small body of international financiers, whose workings are nebulous but effective. The presence of a subtle tyranny

* The last (Fox, Fowler and Co., of Wellington, Somerset) was absorbed by Lloyd's on April 19, 1921.

is felt, while its details are not yet properly focussed. Freedom of contract gives way to a growing extent to the grip of status. The individual cannot advance by his own efforts, so he bands with his fellows to escape from penury. The titanic efforts of organised Labour occupy the universal stage. There are no indications that the intestine struggles of society will lead to progress. On the contrary, there is every evidence that the fate awaiting the world is that of economic disruption.

Who passed the Bank Charter Act of 1844? None other than Manchesterism's greatest statesman, Robert Peel.* The greatest deed of legislative interference in individual liberty came from the very man who is held to be its apostle. The history of Manchesterism coincides with an increasing interference with private banking, and Peel's Act was the crowning feat. Retribution was speedy. Manchesterism succumbed to the assaults upon it, nor could all the eloquence of John Bright save it. The great Factory Act of 1847 showed the extent of its defeat, and the further Acts of 1850, 1864, and 1874 bear testimony to its decline. The Anti-Corn

* Though Peel was a Conservative and supported the Factory Legislation he became a convert to free trade in corn in 1846. Peel and Gladstone are the two Prime Ministers most closely associated with the Manchester doctrine. Peel's bust with its inscription, "The emancipator of Trade and Commerce," adorns the National Liberal Club to-day!

Law League (1838–46) gave England its policy of limited Free Trade, but Cobden (1804–65) was not long in his honoured grave before the Free Trade doctrine was violently assailed. Its supporters are a dwindling number, and the return to Protection is an increasing possibility.

Chapter Five: *From Credit Restriction towards Financial Thraldom*

The subject of the present chapter must necessarily take us out of history into the affairs of the living world. Facts will be less easily controlled and trends must be examined the outcome of which is a matter of conjecture. We shall find that the suppression of the banks of issue has been followed by the emergence, in turn, of the limited liability company, the financial trust, and the financial pool. The financial system has not yet reached its full development, but some of its manifestations are so perturbing that we may well pause and ask whither that system is tending.

Peel's Act was applied in 1845 to Scotland and to Ireland. It soon caused a panic. Its sponsors alleged that the panic was in spite of the Act, but even they were forced to admit that they were disconcerted by its operation.

The panic occurred in 1847. The harvests in 1842, 1843, and 1844 were exceptionally good.*

* See Andréadès, p. 333. It is interesting to note that, while bad harvests are usually thought to be the cause of financial crises, the truth seems to be that credit restrictions generally precede bad harvests. The harvests prior to the credit restriction of 1826 (when notes under £5 were prohibited) were exceptionally abundant

Commerce was flourishing and speculation rife. In 1845 the Irish potato crop failed. In 1846 the failure was worse. Gold had to be exported to purchase cereals. The Bank's reserve fell from £M15 in December, 1846, to £M2½ in April, 1847. The bank rate was raised to 5 per cent., but the panic continued. Between August and October bankruptcies involving £M15 took place. The Bank's reserve rose to £M8, only to fall again in October to £M3½. The rate was raised to 5½ per cent. in October, and advances were refused on public securities and Exchequer Bonds. Consols fell from 84½ to 77¾. The Royal Bank of Liverpool failed, and many other banks followed suit. The Government authorised the suspension of the Act. The effect was magical. The mere knowledge that accommodation could be secured stopped the run.

The Act had done nothing that its promoters had expected. The relation between note issue and bullion reserve had not been maintained. In August, 1846, the note issue was £M20 and the bullion £M16. In April, 1847, the note issue was still £M20, while the bullion had sunk to £M10. Baring was quite unable to explain the extraordinary

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(see p. 99). Those following the Act of 1833, which allowed the joint-stock banks, were similarly plentiful (see p. 102). The harvests of 1842–44 were very good, but when Peel's Act was passed bad harvests resulted.

phenomenon.* Peel himself was obliged to acknowledge the wisdom of suspending the Act.† It had neither prevented speculation nor a financial crisis.

The joint-stock banks now began to challenge the Bank of England in importance. The wings of the banks of issue had been clipped by Peel's Act. Their power to expand their credit facilities was rigidly curtailed. Enterprise had to turn elsewhere for accommodation, and it turned to the joint-stock banks. These had an advantage over the provincial banks in that they were not limited by the six-partner restriction. They could increase their financial resources by issue of new stock. It is true that they lacked the enterprise—the skill in meeting their customers' requirements that the note-issuing banker had always shown. This has been attributed to the fact that the dealings between banks of issue and their clients were of a personal and intimate nature, and that this aspect of banking was bound to disappear when the small banks were replaced by the larger ones. Such a view is erroneous. It was not a question of size which determined the private banker's methods. His interest was to issue as safely as possible as many notes as he could, and he was only limited by his clients' power to build up industry. His activity was naturally directed into

* See Baring's speech, *Parliamentary Debates*, vol. xcv., p. 615.

† See Peel's speech, *Parliamentary Debates*, vol. xcv., pp. 650-672.

seeking out men of sound business ability and assisting to establish them in their business or to extend its scope.

The joint-stock banks were forbidden to issue notes. They had to find a substitute. Economists say that the cheque was a substitute and that its development rendered the note unnecessary. We have seen* that cheque payment was a more primitive form of transaction than note payment, and had disappeared in economic evolution before a better system. Now that the law had suppressed the better form, the lower form again came into use. The cheque, rightly considered, is not a form of credit at all; it is simply a method of payment.† A cheque drawn by anyone against his deposit at a bank does not represent a credit. The deposit itself represents a credit from the individual to the bank. Such credit is useless to industry until the bank puts it at the disposal of producers. This is done by an overdraft, not by an actual loan of gold, but by giving the producer a call upon a certain quantity of gold.

The difference between note credit and overdraft credit is of the utmost importance. To ignore it is to vitiate the whole science of economy. It can be summed up in a phrase. The cheque is centripetal,

* See pp. 75-76.

† Gide, p. 325: "The cheque is not, strictly speaking, an instrument of credit; it is an instrument of pavment."

the note is centrifugal. In other words, the tendency of the note, in normal times of industry, is to circulate further and further from its point of issue, to penetrate through all the industrial layers, from the biggest producer to the meanest wage-earner. The tendency of the cheque is in the reverse direction. Its trend is to be presented for payment or cancellation through the clearing house as soon as possible. Economic history affirms this. The notes of the private bank were more popular even than coin. They vitalised the community. They gave the manufacturer the wherewithal to pay wages until he had marketed his goods. On the other hand, the cheque has never permeated the economic organism. Its use is confined to the upper strata only. It rarely enters into the lives of the workers, and is never used for wages.

Comparison is obscured by the fact that until the recent war practically the only notes in England were those of the privileged Bank of England. These notes in their cumbrous units (£5) were unwanted by the large mass of the people. Compared with them the greater elasticity of the cheque was a boon. Neither cheque nor Bank of England note, however, could hold its own for long under open competition with the notes of an ordinary bank.

The difference in character between the note and overdraft system of credit has led to one important

result. The bank-note by its circulating ability replaces gold and relieves the strain upon the bank's resources. The overdraft has no circulating ability except that which can be obtained by the agency of a clearing house. The effect is that the overdraft system means a much greater strain upon the cash reserve. This had to be met by increasing the cash reserves, not only by getting the shareholders to put up a larger sum total with which to start the bank, but also by encouraging the community to increase its gold deposits.* To this difference is largely due the growth of the deposit system.

The practice of paying interest on deposits in England is comparatively a new one. The Bank of England still refuses to do so, but the Bank of England has practically ceased to be a people's bank at all, if indeed it ever deserved that title. It is to-day simply the bank for the bankers and the State. The joint-stock banks, to protect the overdraft system, were obliged to attract big deposits, and have therefore offered interest on deposit accounts since their formation in 1833.†

* The deposits of English joint-stock banks increased from £M9 in 1847 to £M43 in 1857. (Andréadès, p. 352.)

† See Powell, p. 269 note: "Probably the introduction of the joint-stock banks in 1833 was the beginning of deposit business on a really extensive scale. . . . The older issuing banks, with their small capitals, would not have been justified in accepting deposits to any large extent."

Curiously enough the joint-stock banks advertise the huge amounts of deposits that they owe as a sign of their stability. It is to some extent an index of the confidence that the public has in them, but reflection will show that these deposits are in reality a huge liability which could not be met at any given moment.

The holders of deposit accounts with the Big Five banks have claims on these institutions for some £M1,500 which they have deposited from time to time. This immense sum is not covered by the cash reserve. The joint-stock banks have ceased to hold their own reserves, and have banked in their turn with the Bank of England. That institution has now the only effective reserve in the kingdom, some £M128½.*

A similar tendency has operated in other countries. The Bank of Belgium has the sole cash reserve of Belgium, the Bank of France that of France, and the German Reichsbank that of Germany.

The upholders of the present centripetal system of banking maintain that the concentration of reserves in one national store is a good thing. It must be pointed out, however, that economy is not a national but a world science, and that a nation's political boundaries do not correspond to a community's economic ones. The influence that has produced a centralised store of gold in the State

* September, 1921 (exclusive of £M28½, reserve against currency notes).

bank is not economical but political in origin. It is the result of legal restrictions of note issue.

The centripetal trend has not yet run its full course, and to obtain a clear judgment as to what it really means its further development must be visualised. The cash resources of each country have been concentrated in one national store. The next step will be for these national stores to concentrate in their turn. There is a manifest tendency for them to do so, and unfortunately for England's claim to financial greatness there is no evidence that England will be the venue of that concentration. On the contrary, America has, by virtue of recent events, obtained an undoubted major call upon the world's gold supply, and slowly but surely gold is gravitating thither.* One result is obvious. As

* This is, however, only an acceleration of a movement already traceable in the pre-war period, as the following table shows:

Year.	*Bank Cash and Bullion Reserves in £M (at par).*			
	U.S.A. (including U.S.A. Treasury).	*England.*	*France.*	*Germany.*
1880*	68	28	79	31
1889	99	28	101	59
1907	233	31	107	35
July, 1914	398	38	165	67
1919	625	98	144	54
1921	663	157	143	54

Of the world's monetary gold stock, estimated at roughly £M1,750, U.S.A. holds more than 37 per cent., and its holdings are still increasing, while Russia and Austria have been denuded.

the private individual had cause to regret that he did not get the same consideration from the centralised joint-stock banks that he was able to get from the old banks of issue, so already have the nations of Eastern Europe bitter reason to complain that their urgent need for credits receives no attention. They are threatened with the alternative, either of economic dissolution into primitive agricultural communities, trading only by barter, or of obtaining credits from American financial pools at a crushing rate of interest.

A second result of the centripetal system should be equally obvious, but has escaped notice. The centralisation of credit control that has been going on since the passing of Peel's Act, and kindred Acts in other countries, has had a reflex action upon the whole industrial organism. It has induced that strange phase of modern industry known as trustification. In a subsequent chapter it will be shown that this perturbing result is due, not to an inherent vice of capitalism, as the Marxists believe, but to the unnatural vice of State-restricted finance.

The deposit system was responsible for the most acute financial panic the world has known, which occurred in 1857. The greatest blow was felt in the United States. The great gold discoveries in 1849 had led to a large increase in cash resources and had induced great prosperity. Railway expansion took

place on an unprecedented scale. Between 1849 and 1857 some 21,000 miles of railroad were laid, about seven-ninths of the total railway system of that country. To finance the growing industries banks multiplied from 745 in 1847 to 1,416 in 1857. The statesmen had taken a lesson from England, and had passed Acts imposing limitations upon note issue. So restricted was the note issue that it was less than the bullion reserve.*

Recourse was of necessity made to the overdraft and deposit system. To attract deposits high rates of interest were offered to depositors. The effect was to withdraw the cash resources of the nation from circulation into the banks' strong-rooms. The restriction imposed by legislation prevented the issue of notes to replace the cash so withdrawn. The result was a sudden demand for currency, with a consequent panic. In New York alone, out of the sixty-three banks only one did not suspend payment. Throughout the country there were over 5,000 failures, with total liabilities of more than $M294.

The repercussion reached England, still struggling under the effects of the Crimean War. The demand for gold from the United States led to restriction of

* Juglar, p. 268: "En 1857, par suite de la sévérité des règlements, on ne pouvait accuser l'exagération de l'émission, car elle ne dépassait pas souvent la réserve métallique."

cash resources here. The Western Bank and the City of Glasgow Bank failed. The reserve of the Bank of England dropped from £M10 to £500,000 on November 11, in spite of a bank rate of 10 per cent. Next day the cash reserve was £320,000, and the bank was within forty-eight hours of bankruptcy. Again Peel's Act was suspended. Notes to the amount of £M2 over the statutory limit were printed, but only £928,000 had been put in circulation before the community's thirst for circulating medium was appeased and the panic was over.

The overdraft system of financing industry was not long in showing its limitations. It was efficient only for short-dated credits of a few months. It was a useful method for established businesses, but it did not assist in promoting new enterprises. That function had largely been exercised by the old banks of issue, but Peel's Act had limited their powers. A way out had to be found, unless industrial development was to be stopped.

The remedy was supplied in the first place by joint-stock companies of unlimited liability, but this soon proved unsatisfactory. Industrial evolution was creating business responsibilities vaster than before, both in regard to magnitude and period. An example will show what is meant. If a man fashions a rough piece of wood into a sandal and fastens it to his foot by withies, he receives the

benefit of his labour the same day. If a man erects small brick works and sells his product, he needs small cash resources in the first place, and obtains his return probably within a year. If, however, a joint-stock company builds a railway it requires large cash resources, and its profit will not accrue until some years later. The collapse of the railway boom in 1845 showed the perils to which the investors with unlimited liability were exposed.* In the event of failure they were liable for the company's debts to the extent of the whole of their possessions.

The principle of limited liability was no new one. It had been evolved by the Romans, but could only be exercised under charter of corporation granted by the Senate, which rarely gave it to a trading company. In England the same restriction held. The Bank of England itself was from the outset a limited liability company. The Act of 1694 laid down that the Bank was not allowed to borrow or owe more than the amount of its capital, and if it did so the individual members became liable to the creditors in proportion to the amount of their stock.†

* Duguid, p. 154: "Many innocent men liable for calls had to fly the country, as if they had committed some crime, and to live abroad for many years upon what remnants of their property they could manage to save from the general wreck and from the grasp of the law."

† Gilbart, vol. i., p. 32. See also Powell, p. 303 note. Powell also says (p. 299), referring to the renewal of the Bank of England's

The resistance to limited liability was very great on the part of the established firms, but in the end vested interests had to yield to economic pressure. By the Acts of 1855 and 1862, a certificate of incorporation with limited liability was to be had for the asking. New companies sprang up everywhere in answer to the demand, hitherto suppressed, for industrial expansion. In 1863 limited liability companies were financed to the amount of £M100, in 1864 £M156, in 1865 £M107. No less than 3,480 companies were launched between 1863 and 1866. But when the leeway had been made up, the flotations dropped to normal again. In 1866 the total financed was £M68, in 1867 £M29, and the £M100 mark was not passed again until 1872.*

The limited liability system has continued to grow in volume. Not only does it preponderate as a method of establishing new businesses, but almost every large old-established business has conformed to the new method. In assessing its place in the economic structure, however, it should not be forgotten that the system did not come into prominence until the banks of issue had been doomed to

charter in 1708: "It was imagined that private firms of six persons, or less, working with *unlimited* liability, could not imperil the supremacy of the gigantic new enterprise, armed and defended by its *limited* liability."

* See Powell, pp. 395-6.

extinction. Those banks had shown themselves to be the credit medium between the men of enterprise and the community. Had they been allowed to increase their resources by the abolition of the six-partner restriction, there is no reason why they should not have developed *pari passu* with the industrial side of commerce. The canals of England were dug by the financial aid of private banks, and the railways could have been constructed in the same way. Short-sighted legislation alone presented an insuperable obstacle and caused the growth of the system of limited liability, the defects of which have never been lost sight of by the social student.

The joint-stock banks were sufficiently stable to stand the panic of 1857, and were rapidly challenging the position of the privileged Bank of England. Another crisis was at hand. It occurred in two phases—the first in 1864, the second and worse in 1866.* The events leading up to the crisis were as follows: The American Civil War (1861–65) strained the resources of that country. To pay its way the Federal Government issued non-convertible notes (green-backs). The suspension of cash payment led to a great efflux of gold.† Cotton-growing in the South was seriously affected, with the result

* Juglar, p. 384, describes it as "La plus grave sécousse commerciale des temps modernes."

† Conant, p. 644. The gold exports were in 1862 \$M22, in 1863 \$M57, in 1864 \$M89 in 1865 \$M52.

that Lancashire industry was almost paralysed. The influx of gold into England from America was to some extent counterbalanced by exports to the East. Gold to the amount of £M24 was sent to India between 1862 and 1866. Trade was expanding, the limited liability companies were being floated to an undue extent, endeavouring to reach their economic level, since legislation had delayed their growth. Centralisation of cash resources proceeded rapidly. Deposits which totalled £M63 in 1860 had reached £M91 in 1864. In addition, the banking firms were trying to meet the needs of the expanding industry. Note issue being barred, they had recourse to a system known as "financing" —*i.e.*, issuing accommodation bills on a large scale, not upon actual production, but upon prospective results. A company, instead of issuing shares direct to the public through the medium of a limited company, would deposit its stocks and bonds with a finance company, which on that security advanced the necessary credit resources. This practice of "financing" yielded big profits, and led to many private firms entering into the field. Among these was Overend, Gurney and Company. This firm had had conspicuous success in its earlier transactions, financing cotton operations in U.S.A. and railway operations in Great Britain. It enjoyed immense popularity, and in 1865 was transformed into a limited company.

In 1864 the first stringency occurred. The bank rate was forced up to 9 per cent. The crisis seemingly passed, with the liquidation of the smaller tradesmen. But it left a feeling that the practice of financing was a risky one, and the more prudent finance houses withdrew. Overend, Gurney and Company continued. An action brought by the Mid-Wales Railway led to a judgment on May 9, 1866, that financing was illegal. Two days later the crash came. May 11 is known as Black Friday in financial history. Lombard Street was besieged by a mass of applicants for accommodation. The Bank of England's reserve fell from £M6 to £M3 in a day, in spite of a 10 per cent. rate. The same day the Government wrote to the Bank suspending Peel's Act, and the panic subsided in due course. Again (as in 1847) it was not necessary for the Bank to issue in excess of the limit imposed by Peel.

The crisis further centralised the banking interests by crushing out the weaker banks and the finance companies. It also crushed out many an enterprising tradesman. The failures actually recorded amounted to over £M50, and investments of every description were affected.*

The crisis had one other effect. It brought

* Conant, p. 651: "The simple truth was that the credit of English finance was shaken to its centre."

into evidence the fact that the Bank of England was no longer the big banking influence in the world. The suspension of Peel's Act was urged upon the Government by the joint-stock banks, only the Bank of England's representative on the deputation withholding his hand. The Government could not withstand their influence, neither could the Bank of England. One of the representatives of the joint-stock banks bluntly said to the Bank of England's representative: "I can draw a couple of cheques to-morrow morning which will shut you up at once."

Financial development has since taken a step further. The influence of the joint-stock banks is now secondary to that of the Morgan pool. A similar threat would never be repeated in all its bluntness, but no one can doubt the power that lurks behind the silence.

After 1866 English finance entered into a period of comparative stability. The limited companies expanded in all directions. South America, particularly the Argentine, was fast developing, and the development was largely financed from London. The result was to be a failure which involved the greatest house of the nineteenth century. At one time Baring's reputation surpassed that of all others. Its bills were held to be safer than Exchequer Bonds. The years 1888-9 were exceptionally prosperous.

People sought a good investment for their savings, and the growing prosperity of Argentina attracted them. Flotations for financing industry in that country were controlled by Baring's. Speculation became rife. South Americans took advantage of the position to promote unsound ventures.

Then doubts arose. In the spring of 1890 Argentine securities fell in value. The Bank of England foresaw the coming pressure and raised its rate to 6 per cent. The City financiers strongly objected. The joint-stock banks sided with the financiers and kept their discount rate at 4½ per cent. only. Under this competition the Bank of England was forced to reduce its rate to 5 per cent. and still further to 4 per cent. Baring's were underwriters for a big flotation for the Buenos Ayres Water Works Company, but the public were frightened, and the house was left with the bulk of the issue on its hands. On 8th November application was made to the Bank of England for aid. Investigation showed that the soundness of the holdings in Argentine securities was very doubtful, and the world soon learnt that Baring's had failed. People rushed to realise their securities, and Consols fell sharply.

The crisis was tided over by the action of the Bank of England, which started a guarantee fund to cover Baring's obligations. In a few days £M10 was promised. The bank rate had to be raised to 6 per

cent., but the Bank of France relieved the position by loaning £M3 to the sister institution in England.

The crisis was not as painful as those which had preceded it. It seized upon popular imagination rather by the fall of a great reputation than by the suffering it caused to the community at large. It was the last big crisis in England, and henceforth, the financial world was to be dominated by events in America.

The fall of Baring's has been attributed by some to the accumulation of funds in the hands of financial trusts, an important feature of modern finance. A financial trust is a company that operates by purchasing shares in industrial companies. These trusts originated first of all in a desire for security on the part of the investor. In the early days of joint-stock banking the best form of investment was held to be mortgage on land, which, in a country still largely agricultural, was easily saleable. With the growth of centripetal finance England became more and more dependent on foreign sources for her cereals. Agriculture declined. Land mortgage ceased to be a safe banking investment. The advent of the limited company, in answer to the economic need for long credits, which the overdraft system could not undertake, threw the risk attaching to such investments on to the public. That element of risk was always great, since the public had no

opportunity of thoroughly testing the soundness of the many new issues. Certain financial companies arose, the object of which was to eliminate or reduce the risk factor. The London Financial Society, founded in 1863, spread its holdings over the many railway companies. Its object was not to promote new industry but to profit by established industry. The growing unwillingness of finance to promote new industry is one of the signs of economic sclerosis which was already beginning to invade the English industrial system.

The panic of 1866 showed that the railway stocks were not easily saleable in a time of financial stringency. The investing public therefore turned its attention to other directions. In 1868 the Foreign and Colonial Government Fund was founded. Its object was to lessen risk by spreading its holdings over a number of Government stocks. A similar institution was the Government Stock Investment Company. The higher dividends paid by commercial undertakings led to kindred companies being formed to deal in industrial stock. The Submarine Cables Trust was floated in 1871. This was a trust to deal in a specific form of enterprise, but it pursued the method of distributing its holdings. Attempts were made to form a bank share trust, but the banks protected themselves by refusing to allow their shares to be sold to such

bodies. In 1884 the Mercantile Investment and General Trust was formed on more general lines, and following upon that there came an increasing number of similar formations up to 1890, when the Baring crash gave a temporary check to the new movement.* The movement soon recovered, however, and to-day the Stock Exchange list shows financial trusts in every branch of industry. There are, among others, mining, rubber, railway, cotton, telegraph, estate, and general trusts.

Although these trusts were formed originally to reduce the risk attaching to investment, that aspect of their activity has fallen into the background. When they first appeared the presumed safe investments were few and dear. Consols were high in price and small in yield. The growth of State and municipal finance has led to a multiplicity of such investments, and has effectively transferred the savings of the timid investor from productive enterprise to the unfathomed pool of public debt. Since 1890 the Trusts have catered not so much for safety as for dividends. They have become underwriters for fresh flotations, usually not for new enterprises but for the extension of old enterprises. In Stock Exchange jargon they are known as the "shops."

* Among the victims was the London and Globe Finance Corporation, whose fall caused some thirty members of the London Stock Exchange to go into default.

Their ability to obtain inside information and their control of cash resources makes them a powerful factor in the financial world. If a trust buys, the stock is held to be going into good hands, the news gets round, and a boom ensues. If a trust sells, it is held that the industry whose stock is unloaded is in a bad way, and depression follows.

It has been maintained that the financial trusts have introduced a stabilising element in the value of securities. They act as a kind of barometer, by the study of which one can gauge the industrial situation. It would be difficult to prove this. Since the advent of the financial trust, with its power of enhancing and depressing the values of stocks and shares, the wildest fluctuations in values have occurred, boom after boom has been engineered, and slump after slump has followed. The small investor is without protection, as he is beginning to learn to his cost. He can only cease to rely on his own judgment and commit his slender resources to the care of the trust companies.

If the normal rate of interest be 5 per cent., and manipulation of the market enables share values to be enhanced or depressed to a greater amount, it is obvious that there will be a constant incentive to gain, not from production, but from manipulation. Experience shows that such market manipulation is an increasing aspect of the financial system.

The transit of the world's financial centre from England to America is not yet an acknowledged fact, but there are many indications that this has already taken place. At one time the most powerful financial influence in the world was wielded by the European Rothschilds, with the English branch at their head. In the latter part of last century stories of fabulous wealth, accumulated in the hands of American financiers, eclipsed the legendary tales of bygone ages, the splendours of the "richest East", and the envied fortunes of Europe's magnates. The names of Vanderbilt and Astor became household words, to wane in glory before the greater lustre of Carnegie and Rockefeller. These in turn are dimmed by the transcending brilliance of the Morgan family.*

It is significant that while England was the undisputed centre of the world's finance, crises developed their greatest intensity in this country. France and Germany suffered only their secondary repercussions. Fluctuations in bank rates were less feverish there than in England. Latterly the greatest crises have been in America, while England has suffered prolonged periods of financial depression.

* According to Gide, p. 191, Rockefeller and J. P. Morgan are alleged to have controlled, prior to 1914, a totality of enterprises (railways, mines, petroleum wells, iron works, banks, etc.) to the value of £5,000,000,000.

The English crisis of 1890, great as it appeared at the time, was dwarfed by its sequel, the American crisis of 1893. The first shock was felt at the point furthest from the centre. The distrust caused by the failures in Argentine caused a sale of holdings in Australia. The withdrawal of cash resources was followed by the failure of many Australian banks. The repercussion was felt in Germany, Austria, Italy, France, and even Turkey. It caused the closing of the mints in India and the shutting down of one-third of the silver mines of the world.

The growing distrust led to a refusal by European financiers to invest further in American industry. The interest on old investments was no longer reinvested in the country, but was transmitted to Europe. The result was an unquenchable drain of gold from the American banks. The enforced circulation of silver by the passage of the Sherman silver law further operated to drive out gold. The gold in the United States Treasury sank from $M326 in 1889 to $M171 in 1896. The result was that in the period June to August, 1893, no less than 141 banks suspended payment. The business failures in 1894 numbered over 15,000, and more than one railway system went into liquidation. Money rates jumped in one day from normal to 75 per cent. The crisis was due not to over-issue of

notes, but to the deposit system and to State restrictions.*

Financial history after the panic of 1893 is largely that of the financial pools. A financial pool is formed by the pooling by big financiers of the resources of the financial trusts and the industrial companies that they control, in furtherance of an agreed policy. The Standard Oil Company, in which John D. Rockefeller was the leading spirit, played an important part in controlling industry in America, until the mastery passed later to the Morgan interests. J. P. Morgan's interest in Standard Oil was at first a minor one, but apparently increased in course of time. It was, however, owing to his obtaining control of the banking system that he was able to become the world's dominating financier.

* Conant, pp. 680-683: "Those who had fancied themselves in possession of an assured income from their stock holdings found their wealth turned to ashes in their hands. . . . The financial crisis of 1893 was a striking illustration of the truth that bank-note circulation plays but a trifling part, or none, in promoting crises. The National banks had been contracting their secured circulation . . . but individual deposits were multiplied. . . ."

"Many banks throughout the West were obliged to suspend, because their resources were not within ready reach. Out of a total of 158 National banks which were forced to suspend payments during the year ending October 31, 1893, eighty-six were authorised to resume business within a short time, and not one of these was east of the Ohio or north of the Potomac. This is the best proof that these Western and Southern banks would have been able to maintain their solvency if their cash reserve had been in their own custody."

In February, 1895, he was associated with the London Rothschilds in a syndicate to supply 3,500,000 ounces of gold to the United States Treasury in return for Government bonds. The panic of 1893 had led to a constant outflow of gold, which had caused prolonged trade depression. Morgan allied himself with the gold-shipping firms in an attempt to stabilise the exchange price of the dollar so as to keep gold in the Treasury. The attempt failed in July, 1895. He nevertheless competed to buy a further issue of bonds for the same purpose, and his syndicate obtained \$M38 of them out of an issue of \$M100.

In 1899 he was associated with the Standard Oil interests in the flotation of the Amalgamated Copper Company, the unsavoury story of which has been graphically described by the originator of the proposal.*

In 1900 came the great fight between Morgan and Hill for the control of the Northern Pacific Railway. The price of the stock under constant buying rose from $43\frac{3}{4}$ in September, 1900, to 180 in May, 1901. It then became evident that a corner had been manipulated in the stock, which rose to 1,000! Operators were obliged to throw all other securities into the market to cover themselves, and prices slumped. The money rate rose to 75 per cent. in

* T. W. Lawson, *Frenzied Finance.*

one day, and the morning after the crisis it was back again at 3 per cent.

In 1901 Morgan floated the United States Steel Corporation, financed at no less than $M1,400. As underwriters Morgan and Company appear to have made a profit of $M12½ on a sum of $M25. The unfortunate shareholders lost heavily, the $100 shares ultimately sinking to $10. The production of the United States Steel Corporation increased by only 40 per cent. in the period 1901–13, while of its rivals, the Bethlehem Steel Company increased production by 3,779 per cent. and the Inland Steel Company by 1,495 per cent. in the same period !*

In 1902 Morgan formed a syndicate to carry through the conversion of the United States Steel Corporation bonds. Apparently the result of this operation was to give the underwriting syndicate some $M7 as a reward for raising some $M13·2 for the Corporation. The deal was made the subject of an action at law, on the ground that it was a deliberate attempt to " milk " the shareholders for the benefit of the underwriters, with whom many of the directors were associated. The directors won a complete legal victory, while grave reflections were cast upon the motives of the shareholder who challenged their action. There is, however, little

* See Ripley, p. 103.

doubt that the legal verdict was the reverse of the moral verdict.*

The period 1902–07 was noticeable for a great money stringency in the United States. This was particularly evident in the autumn when the crop movements took place. The reserves of the New York banks fell below the legal limit in September, 1902, twice in 1905, four times in 1906. In 1905 the rate for call money touched 125 per cent.

The same period was remarkable for a growth in the State banks. The National banks, incorporated under the Federal laws, had proved insufficient for the country's needs and banks developed outside the ambit of those laws. They lacked certain of the privileges of the National banks, but they supplied a want. In 1900 their number was 9,519, in 1907 it reached 13,317. Their resources increased from $M5,841 to $M11,168, and their cash reserves from $M221 to $M392.

In 1907 occurred the most sensational panic America had ever known. The long period of depression had given place to a period of trade expansion, and from 1904 onwards speculation for a rise in prices took place. The increasing trade led to a demand for cash for internal circulation. Gold was imported from Europe. In October to December, 1907, some $M124 was imported, yet the

* See Ripley, p. 256.

reserves of the New York banks declined by $M61. Some $M300 was absorbed in internal circulation. The crash came very suddenly. A financial pool had gambled in copper and had involved certain banks in its operations.* There was a collapse in the stock market. Buying power disappeared mysteriously.† The shrinkage in values was no less than $M5,000. The clearing-house banks refused to clear for the banks involved in the copper pool. The position on the Stock Exchange became most critical. Its president, Mr. Thomas, called upon Morgan at 2.20 p.m. on October 24, and informed him that the Exchange must close unless money was forthcoming. The same afternoon Morgan summoned the presidents of the big New York banks, and pledged a fund of $M25 to relieve the situation.

The generally accepted view is that Morgan acted as a public benefactor in the matter. The more reasoned inference would appear to be that he had carefully manipulated a panic, and stepped in exactly at the moment when he could derive the maximum advantage.

The sequel is interesting. The Secretary of the United States Treasury, Mr. Cortelyou, hurried back to New York and insisted that the financial interests of the country should be united. The

* See Chapter VIII.

† Conant, p. 711.

one man capable of assuming control was Morgan, and he dictated his own terms. Large deposits of public funds were transferred from the Treasury to the National banks, to the extent of $M35 in New York alone. With the aid of these and other resources Morgan proceeded to help the jeopardised banks, but only upon the condition that he should replace certain directors and managers by men of his own choice. In addition, the circulating medium of the country was increased by the issue of certificates by the bank-clearing houses. These were issued to the amount of $M100 in New York, $M37 in Chicago, $M13 in Philadelphia, and to smaller amounts in other cities.

The crisis passed as rapidly as it had developed, but it had done incalculable damage not only in America but elsewhere. The English bank rate rose from 4½ to 5½ per cent. on October 31, to 6 per cent. on November 4, to 7 per cent. on November 7, the highest mark since 1873. In January, 1908, it fell again to 4 per cent. The result of the crisis was to make Morgan the supreme controller of the most powerful banking system in the world.

The crisis was not due to excessive note issues. It was due to that economic arch-folly, State interference in note circulation. The crisis passed as soon as the banks issued clearing-house certificates.

This is affirmed by a celebrated modern economist, who yet, curiously enough, supports the heresy of State control of banking.*

Morgan took advantage of his triumph in 1907 to secure the passage of the Aldrich-Vreeland law in 1908, and of the Federal Reserve Act of 1913, which placed the control of the banks of the United States under a board of seven people. This Act forced the National banks, and practically compelled the State banks and Trust companies, to place their ultimate reserves under the control of the above-mentioned Board. The outflow of public expenditure during the Great War has somewhat obscured the working of the new system, but the general result is clear. The nations of the world are dependent upon America for credit, and Ameri-

* Gide, p. 438: "The fourth method consists in obliging banks to *guarantee the notes they issue by reliable securities*, as a rule by certificates of Government stock, which must be equal at least in value to the notes. . . ."

"This system was devised by the Government during the Civil War of 1863, as much to sell off the Government bonds, which the State was obliged at that time to issue in milliards, as to guarantee the notes. . . . To-day, as the debt is in great part repaid, Government bonds have become scarce, and it is difficult for the banks, which are increasing in number, to find the necessary amount. . . . Thus the issue of notes in the United States has become very difficult. There is no elasticity in the circulation. This is what aggravated the crisis of 1907. It was not gold that was demanded —the public would have been quite content with notes. But the banks could not issue them. . . ."

can finance is controlled by the Morgan pool. As far as can be seen at present, America is itself in the throes of a credit stringency, and the hope that Europe cherishes of obtaining adequate aid upon reasonable terms from the United States would seem doomed to frustration.

The financial pool differs from the financial trust in one important respect. The trusts are definite organisations, registered under law. Their actions are, to some extent, controllable. The pools are merely shadowy groups of undefined personalities. They are created and dissipated at the arbitrary decision of financial magnates. They operate through their control of the resources of the banks and the financial trusts. They induce artificial inflation and artificial depression. They work their will upon the world's industrial needs. They transfer their activities from wheat to public debt, from public debt to oil, from oil to sugar, from sugar to railroad systems. No market can withstand their influence. They enhance the gigantic fortunes of their members to transcendent dimensions. The determining influences of the world's destinies are within the control of a few men, who can be numbered almost on the fingers of the hand. Within this narrow circle the fight for supremacy goes on. Pools are broken and reformed as power fluctuates from one side to another. Under their operations

rich men have found their envied wealth crumble to nothing. The dominating pool at present is the Morgan pool. Financial control may pass from it to other and more forceful pools in future, but the tendency is centripetal and financial power becomes daily more concentrated. The crowning point is not yet reached, but the end is in sight. That end is the control of the world's resources in the hands of a small group of financiers, a despotism more monstrous than the world has ever known.

Chapter Six: *The Essence of Cash and Credit Finance*

The term credit is to-day upon the lips of everyone. An international scramble for credit supply is in process. Some of the competitors are more favourably placed than others. Eastern Europe appeals to Western Europe for accommodation. Western Europe appeals to England. England placed a few faint hopes upon the United States, but they were rudely dispelled. America is suffering from a credit scarcity, and cannot satisfy her home demands. The New York merchants, dependent upon their European trade, have sought in vain for sufficient long credits to restore that trade to its pre-war conditions. Money rates have proved prohibitive, and the American bankers dare not tie up their credit facilities for any lengthy period. The demands upon them from the interior of the country are so pressing that a stringency pervades the whole structure. New York money rates in December, 1919, rose to over 20 per cent.

In the absence of credit facilities from America the position of Europe is critical. Loans can only be raised by the various Continental Governments at the unprecedented rate of over 9 per cent. Houses cannot be built. Employment cannot be found.

Food supplies are jeopardised. Yet in spite of the gravity of the problem there is no real appreciation of what credit is.

As a preliminary to a correct grasp of the question we must ascertain what is the real essence of cash money. Let us then retrace our steps into an era where we can exercise a less disturbed vision. History tells us that cattle once served as money, and was superseded by the metals, copper, silver, and gold in turn. The modern economist has analysed gold in its economic aspect, and has found that it possesses certain qualities which render it the most suitable commodity to serve as money.

These qualities are variously stated. One of the most brilliant of modern economists* lists them as follows: (1) Ease of transport; (2) durability; (3) identity of quality; (4) difficulty of counterfeit; (5) divisibility (including fusibility). The first renders gold capable of being brought to market, the second renders it possible to conserve it for the market, the third renders it easy of valuation, the fourth makes it difficult to deceive the purchaser, the fifth makes it possible to market it in any quantity without altering its value.

It will be observed that cattle possess some of the qualities set out above, though to a less extent than gold, while others, such as divisibility, they

* Gide, p. 284 *et seq.*

cannot be said to possess, without doing violence to the ordinary meaning of language. Yet cattle served as money. Copper again possesses all the above qualities, though to a less degree than gold. In its time copper also served as money. The question naturally arises, What was the essential characteristic of these commodities that determined their use as money, and what cause decided that they should each in turn be superseded?

Reflection will show that all the qualities enumerated above are but separate rays that can be brought to one focus. They each serve to give the commodity embodying them a certain advantage in exchange over all others. In combination they determine that the commodity in question is the most exchangeable commodity.

This, then, is the explanation. In any economic society commodity-money will take the guise of that commodity which the society finds to be the most exchangeable one.

Gold is to-day the most exchangeable commodity. The possessor of gold can always exchange it for goods. The possessor of goods cannot nearly so easily exchange them for gold. Hence gold is the cash money of the community.

We are so used to the existence of gold as the basis of cash money that it appears to have no possible rivals. Yet its present triumph is of quite

recent date. In England gold finally superseded silver in 1816, the law, however, simply codifying an already established economic triumph. Throughout the rest of the world the triumph is within living memory. Portugal adopted gold in 1854, Germany in 1873, Scandinavia in 1875, Roumania in 1890, Austria in 1892, Russia and Japan in 1897, and Peru in 1901. In the Latin Union (France, Italy, Belgium, Switzerland, Greece) the triumph of gold has not yet met with legal recognition, neither has it entirely in the United States of America, Mexico, Holland, or Spain. In none of these countries, however, has any serious attempt ever been made to restore silver to an equality with gold without disastrous results. In China and India silver is still the most exchangeable commodity, although the trend is undoubtedly towards its supersession by gold.

It should not be supposed, however, that the pre-eminence of gold as commodity-money has not been questioned or that its future is assured. The threat has come not from the dwindling power of its former rival, silver, but from another quarter. Last century Russia made an attempt to introduce a currency of platinum, but failed. The latter metal at that time was closely equal to gold in value, weight for weight, and it had no economic superiority. Its inferiority in use was marked. It was

unknown to the mass of the people, and almost its sole use was in the manufacture of scientific apparatus for the chemical laboratory. To-day it has invaded the industrial world. It is used in the making of electric lamps, it enters into the mouths of people in the form of dental fillings. Its increased value has given it an economic advantage over gold, in that its cost of transport is lessened. Moreover, it is superseding gold as an ornament. Platinum as a setting for diamonds is superior to the yellow metal.. Already in America it is in vogue for engagement rings. Harmony of colour has naturally decided that wedding rings should be made of the same metal. Hence it is possible that platinum will win that place in popular esteem now occupied by its more tawdry rival. One potent factor is at work. International and interstate balances have grown in volume, and to settle them by the transport of gold is a costly affair. As platinum is some three times more valuable than gold, its use would mean a proportionate saving. It is, however, unwise to hazard too much upon such a point. The source of platinum supply in pre-war days was Russia, now excluded from the world's markets. At present the supply comes chiefly from Colombia. If Russian industry is re-established platinum will probably decline in value and its rivalry be less dangerous.

According to Professor Jevons,* money is used—(1) as a commodity; (2) as a store of wealth; (3) as a medium of exchange; (4) as a measure of value. This list is incomplete. Money is also used (5) as a medium of credit and (6) as a basis of credit.

The origin of the cash nexus in economic society lay in the fact that in an exchange both parties were normally the gainers. If a man were a better boot-maker than cloth-weaver, it would pay him to make boots in exchange for cloth, provided that he could find a cloth-weaver who needed boots, or that he could use a mechanism which would enable him ultimately to obtain the cloth that he wanted. That mechanism was cash money. He sold his boots for cash to whoever needed boots, and he waited until he found a weaver who had cloth to sell. By this means he was enabled to devote himself more and more to that occupation which he had made his special branch of industry. In doing so he was promoting to a small degree the system known as the division of labour.

The division of labour proved to be a great industrial advance. By enabling men to specialise on one particular trade it called new industries into being. As the economic machine grew stronger, greater developments could take place. At the same time, it caused an increasing strain upon the

* Jevons, chapter iii.

cash resources of the community. This vital consideration has not been sufficiently emphasised by economists.

In the feudal days the great bulk of the people were peasants, who grew their own food and made their own rough clothes. Let us picture a typical village of some hundred souls living in cottages grouped round the feudal manor. While the men toiled in the fields, the women spun and wove. The wool clipped from the sheep was made into rough garments without the intervention of any cash transaction. Money values were less than now. A sheep in the eleventh century cost only 5d. The clothes of the peasant probably closely equalled a sheep in exchange value. The total value of clothing consumed each year in such a community would perhaps not be more than some £2.* Now picture the same village at the height of the craft gilds (A.D. 1300). The cash nexus has largely diffused through society. The peasant

* An over-estimate. The live-stock of a whole village was only worth £8 odd.

	£	s.	d.
2 oxen	0	5	0
220 sheep at 5d.	4	11	8
24 pigs at 8d.	0	16	0
6 horses at 10s.	3	0	0
	£8	12	8

See Cunningham, p. 171, note.

sells his produce at the market town and buys his clothing. The value of an outfit of clothes in the meantime has risen from 5d. to 2s. To buy one outfit of clothing for 100 people per annum would probably need £10 in cash, if all purchases were made at once. But another important factor has to be considered. The clothing industry has been specialised. The wool must be sold to the carding industry, from there to the spinner, thence to the weaver, and in turn to the fuller and dyer, and finally to the tailor. The woollen clip, instead of being made into clothes without any cash intervention, causes a call upon cash resources some five or six times before it reaches its final destination. If, therefore, the total value of clothes consumed per year in the village be £10, the annual cash demand created in this branch of industrial life alone is some £50. The figure is somewhat exaggerated, it is true, since carding, spinning, weaving, fulling, dyeing, and tailoring were not so separated as is suggested above. It serves, however, to show how the division of labour caused a strain upon the cash resources. An extension of this line of thought will suggest how important the strain upon cash was bound to become. Not only did the peasant buy clothes, but he bought implements, boots, building materials. Again the clothing gildsman bought from the other gildsmen. Cash was required after

every output of product in order that sale could take place. Specialisation of industry, or division of labour, went on apace, with an increasing call for cash. Some materials were perhaps to pass through the hands of some fifty purchasers before the final product was obtained.

Let us translate the above argument into general terms. A primitive feudal community produced everything for personal consumption. Assuming, as a basis, that the total money value of all the products was £100 a year, nevertheless the cash requirements of such a community were nil. Now, under the influence of the division of labour, a change of system takes place, and each producer produces, not for personal consumption, but to sell. One result is increased industrial efficiency. The total value of the product is increased, let us assume, to £1,000. The partially manufactured goods must pass from purchaser to purchaser at increasing values before they reach the state of final product. If the number of transfers involved is five on an average, the cash transactions of the community have increased from nil to £5,000 per year. This figure again is an exaggeration, in that it makes no allowance for the fact that the product is enhancing its money value at each transfer. The wool from the sheep's back might, for example, be sold to the carder for £1, by him to the spinner for £2, and,

when spun, to the weaver for £3, then to the fuller for £4, to the dyer for £5, to the tailor for £6, and to the final purchaser for £7. A nearer estimate would probably give £2,500 as the total amount of the cash transactions. The year's cash payments of the community will then have increased from nil to £2,500. But the process still continues. The total produce in another century has increased to a money value of £2,000; the number of independent stages has doubled. The cash transactions per annum will have quadrupled to £10,000, since the £2,000 worth of goods will have to pass through the hands of ten purchasers at an average price of £1,000. The conclusion is, therefore, that the yearly cash transactions of the community will increase at a much greater rate than the total annual value of the produce.*

The way out for the community is either—(1) to increase its cash resources; (2) to speed up the circulation of its stock of money; or (3) to find an effective substitute for cash money. Economic history shows that a progressive community will have recourse to all three methods.

There are, however, serious limitations to the first

* How great a call for money transactions the division of labour entails is shown by the returns of the Cheque Clearing House. In 1919 the cheques cleared amounted to no less than £M28,415. This is exclusive of cash and note transactions.

two of these methods. The increase of the cash store is ultimately limited by the discovery of new mines and by the standard of mining engineering attained. The circulation of cash money depends upon the system of transport, the state of the roads, the custom of paying wages. The number of times cash can change hands in a year is not capable of indefinite increase. Money must be immobilised for certain purposes. It must be kept back to pay the weekly wage bill. It must be transported from one industrial centre to another. While in transit, it is temporarily unavailable for cash payments. The principal method of meeting the growing demand will therefore be to have recourse to the third method. The need of finding a suitable substitute for cash money to meet growing requirements is the origin of credit.

The Economist describes credit as an exchange of present for future wealth. The Socialist regards it as a mere book-keeping transaction. Both are to some extent correct, but both have ignored an essential point. They are describing the ideal, without regard to the real. Credit is indeed largely a book-keeping transaction. The Clearing House enables a large mass of credits on one side to be cancelled against an equal amount on the other. Ideal credit is the exchange of present for future wealth. The credit extended to the manufacturer

is a claim upon the commodities already produced by him and by its use he is enabled to produce further commodities and apply the proceeds from their sale to cancel his obligation.

Underlying the whole superstructure is, however, one point of prime importance, and that is the store of gold. No credit is advanced to-day that is not directly or indirectly a call upon gold. A bank-note is valid because it is a call upon gold on demand. In Europe the call is indirect for the great mass of the people, because the note is practically inconvertible. But the note can be used to buy American dollar notes, which are convertible, and the value of the European bank-note is determined in the last resource by the ease or difficulty of obtaining gold for it from the American Treasury or National banks. The cheque is an evidence either of a deposit or an overdraft, and is a call upon the bank's stock of Treasury or bank-notes. It is therefore an indirect call upon gold. The bill of exchange is not really a credit instrument at all. It is rather collateral security based upon goods, by which the merchant obtains from the broker, either in notes or cheque, a call upon the world's gold store.

When the broken nations of Europe appeal for credit, they are appealing, not for a mere book-keeping transaction, nor for an exchange of future against present wealth. The book-keeping trans-

actions could be done as competently by them as by anyone else. Their present wealth exists in the form of their railways, their mines, their factories. Their future wealth could be supplied by their own energies but for the one determining fact, which sterilises their action and reduces them to economic impotence. They have lost their call upon the world's gold store.

The credit of the various countries is not related to the fertility of their lands, to the richness of their mines, to the size of their factories, nor to the energies of their people. Their lands may remain untilled, their mines unworked, their factories empty, and their people idle. Their credit is related to the amount of gold available immediately or in the near future to support the vast mass of paper credit in existence.

When industrial society had reached a certain pitch of development, the need for credit emerged. In its earliest form it was merely a desire for security. Cash stores were so great that they could no longer be kept safely in the merchant's shops. The merchants could not always use them immediately in commerce. They deposited them at the goldsmiths'. Experience showed that cash economy could be effected by the use of merchants' gold-deposit notes instead of actual gold, and further experience proved that greater economy was attain-

able by use of goldsmiths' notes. The goldsmith's note superseded the merchant's because it was more exchangeable or circulating. The credit of the goldsmith stood higher than that of the merchant; he was in the eyes of his community the more creditable person. The more circulating form of credit ousted the less.

The private banks followed the economical experience of the times. The need was for a circulating form of credit to supplement the cash resources. Experience had shown that in England the most convenient coin was the pound sterling. This was confirmed by the fact that other nations used a coin of somewhat equal value. The private banks therefore wisely issued the £1 note and supplemented it by smaller notes. The Bank of England was privileged and aristocratic. It preferred rather to teach than to learn. It issued cumbrous notes of £20, which people did not want. Therefore the circulation of the private banks invaded the sphere of influence of the Bank of England. The flimsy six-partner firms challenged the powerful monopolist. To protect itself the Bank reduced its notes to £5, and forced its rivals to increase theirs in value. World experience rapidly went against it. Other nations successively reduced their notes in value, but the Bank of England remained obstinate. The Great War of 1914 found it in an impossible posi-

tion, and the State protected the Bank's dignity by issuing £1 and 10s. notes through its agency.

The issue of paper money is an automatic attempt on the part of a community to escape from cash stringency. Metallic money owes its position to the fact that gold is the most exchangeable and, therefore, the most readily circulating commodity. It can only be replaced by an instrument having equal or greater power of circulation. The sovereign circulates because it is of known worth, usable in convenient amounts. The private notes circulated because they were the closest approximation to the sovereign within the reach of the community. The folly of the State in limiting the issue of such notes to small and obscure firms prevented the notes from having that backing which ordinary economic influences, if allowed to operate, would have produced for them. State wars filched from them, by the drain upon cash, the small backing that they had.

The cause was misinterpreted, and legislation was passed to limit any increase of circulating credit.

The Currency School tried to bind the community down to the cash basis. They simply diverted the economic stream from a natural to an unnatural channel. Circulating credit was no longer available, so non-circulating credit had to be used. The whole effort of finance since the passing of Peel's Act has been directed to making credit circulate.

The cheque-overdraft system is a personal system, not a circulating one. The Cheque Clearing House has only succeeded in giving it a semi-circulating character. The strain upon the cash and credit resources of the community has been constantly growing. It has only partly been met by gigantic and unnecessary efforts. The deposit system has centralised the cash resources, but has never been broad enough as a base to allow an overdraft credit system sufficient for the community's needs. The result has been obvious. On every occasion that industry has expanded, the overdraft system has broken down. Expansion of industry means a larger wage-roll, a demand for cash for internal currency. That in turn means a withdrawal of deposits, which causes a restriction of credit. This restriction causes a collapse of industry. Centripetal finance dare not confess its failure, and talks in ponderous terms, but without meaning, of over-speculation.

The civilised world has suffered constantly from a credit stringency. The defect is obvious in an acute form to-day over Continental Europe. It is less obvious in England, except to the producer, who is being forced to stop production, discharge his workers, and face bankruptcy, because the banks are withdrawing his overdraft. It is still less obvious in the United States of America, where, however, the

Federal Reserve banks are drawing on Europe to counterbalance the demands upon their gold stores caused by the country's internal needs. Statesmen and bankers deliver homilies about the dangers of speculation without apparently realising that there is no hard-and-fast line between speculation and enterprise, and that undue checking of the one means the destruction of the other.

The scarcity of credit, however, is not purely a war phenomenon. It is simply presenting itself in a more acute form now than formerly. The scarcity is artificial. It needs none of the ponderous phrases of the economist to teach the masses the meaning of scarcity. During the war certain commodities, sugar or matches, for example, were scarce. The result was that the wealthy classes were in a privileged position. They could obtain such commodities when the poor could not. The shopkeepers no longer exerted themselves to find consumers, but waited for the consumers to come to them. Then they parted with the valued commodity only to the privileged few. Matches could be obtained by old customers, and by new customers who were prepared to bring in business by purchasing quantities of tobacco. The same held with respect to sugar.

Precisely this condition has been normal with regard to credit since the strangling of the private banks of issue. The old country banker tried to

extend his issue with his clients. He exerted himself to find safe points of issue for his notes. The cheque-overdraft banker does not do so. He waits for the customers to find him. He treats them cavalierly. He reserves his credit for the favoured few, or extends it exceptionally to a new client who is prepared to bring in big business. The inability of cheque-overdraft credit to expand proportionately to the needs of the community has had dire results. It starved British and Irish agriculture, and made us dependent upon extraneous sources for food. It ruined our smaller business men, and drove us into the arms of the trusts. It made unemployment a constant aspect of modern life.

The cheque-overdraft system is a failure because it lacks the one fundamental property of economic finance, circulating power. It has only been able to retain a certain degree of that quality by a constant process of withdrawal. It long ago ceased to pretend to finance agriculture. It has since refused to finance new industries. It has made its commitments of shorter and shorter date. At one time merchants could obtain accommodation for six months, now the period is generally three months, and even the three-month bills which the banks accept from the brokers have partially matured before they are taken up. The Bank of England confines itself practically to seven-day bills.

The inevitability of such a withdrawal was clearly foreseen by the old private bankers, but their warnings were not listened to.*

The lack of circulating power in the cheque-overdraft system has not only led to a withdrawal of banking credit from agriculture, from new industries in favour of established concerns, but it has led to discrimination with regard to the latter. The banker is harassed by the need for conserving the deposits. The cheques are constantly being presented for redemption. In stable periods they cancel each other mutually in the clearing house, leaving only a small balance to be paid in gold. But stable periods are becoming less constant in industry. The slightest instability causes a big demand upon the gold store. Growth of internal trade means a call upon gold for internal currency. Growth of external trade needs a similar call from abroad. Cheques and notes are presented for redemption in gold. If such redemption is prohibited in internal transactions by suspension of

* Powell, p. 441: "A banker (belonging to a very great and respectable firm in Norfolk) told H. W. Hobhouse that if all the local note issues were suppressed and one uniform issue established, he would not be able to keep money in his own district and lend it to the farmers at 5 per cent. It would all go to the large marts, Liverpool, Manchester, and so on. . . . It really did go, for Vincent Stuckey told the Committee that deposits went from country bankers' coffers to London, wherever interest ruled high."

cash payments it is accomplished indirectly. Exchange on America is bought. The pound falls and the dollar rises. The dollars so bought are redeemed in gold, and the American call upon the English gold store is increased.

The strain upon the world's gold stores is constantly increasing. It could only be met effectually by permitting the use of a medium of equal or greater circulating power, the private bank-note. This is forbidden by law. The remedy has been sought therefore by loaning credit only when collateral security, easily convertible into cash, is offered. The most readily convertible collateral under the present system is not true wealth, not the factories or the products of industry, but artificial claims to dividends, those stocks and shares which enjoy an open market. Hence the banks lend only to persons who can offer gilt-edged security.

What, in effect, is the result of such an operation? If credit is only extended to those who already possess convertible titles to property the outcome is obvious. The gold-controlling class has a constant advantage over the rest of the community. The owner of dividend-earning bonds is granted further credit. The owner of real, but not readily saleable, wealth is denied it. There is accordingly a constant gravitation of wealth into the possession of the

holders of saleable titles to dividends.* Centripetal finance must preserve its call upon gold. It does so by loaning credit to those who possess the call upon gold. The call upon gold necessarily concentrates into fewer and fewer hands.† That industry is stifled, that competent producers must remain salaried employees, that the labourer sees no outlet from the drab existence of wage-earning, these facts weigh as nothing compared with the necessity of conserving the soundness of a financial structure which is built upon an unsound basis.

* Gide and Rist, p. 463: "Under the joint stock principle the right of property is simply reduced to the possession of a few strips of paper giving the anonymous owner the right to draw dividends in some commercial concern or other."

† This tendency naturally shows itself most strongly at the centre of the centripetal system, the New York financial area, as may be seen from the testimony given before the Joint House and Senate Agricultural Committee by the former Comptroller of the Currency, Mr. J. S. Williams, a member on the Federal Reserve Board during the Wilson Administration. He stated that while a member of the Board he heard much talk about forcing the farmer to sell his wheat, the cotton planter his cotton, the cattle raiser his live-stock, the wholesaler or retailer their stocks of goods, and added: "I do not recall a single occasion during the past year or two of deflation when the Board ever discussed the importance or desirability of requiring the big banks of New York City, some of which were lending millions of dollars to their own executive officials on highly speculative securities and to big syndicates in which those officials were actively interested, and which those banks had been carrying for months and sometimes for years, to liquidate a portion

Let us turn to another aspect of the question. Credit should be synonymous with trust. An act of credit means that one person lends to another, with the trust that the loan will be returned. There can be no compulsion in the matter at all. Otherwise the transaction is no longer one of pure credit, but is overlaid with coercion. The most primitive instinct in man is distrust. Lowly organised communities hoard their savings—hide them away wherever they can find an imagined safe place. Division of labour means trust in someone else, that his labour has produced something which is worth buying. It is interdependent upon the use of money. The growth of cash resources leads the community to the state in which hoarding is no longer secure. Surplus gold must be trusted to other persons to mind. A further step in economic progress shows the best use for saved money is not in giving it to

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of those loans, in order that by doing so those banks might have more money to supply the legitimate use of trade and commerce." He further stated that early in 1920, while the speculation was under full headway, he wrote to the Federal Reserve Board protesting against the extent to which the funds of the system were being used to fan the fires of speculation, and gave an instance "where the Federal Reserve Bank of New York was lending to one institution about $M130, twice as much as the Federal Reserve Bank of Dallas was lending to all the thousand member banks in that great district embracing the State of Texas and parts of Louisiana, Oklahoma, New Mexico, and Arizona."

another to hide, but to use in commerce. This marks a tremendous advance. Distrust has been converted into trust. Socialising forces have been brought into play. But trust in others to use one's savings in commerce has its limitations. The money must be returnable. That can only be secured if the borrower uses it wisely—that is, puts it to productive purposes. For if he squander it in non-productive uses, the lender will not be in a position to obtain repayment.

This conception of credit is important because all the modern trends of so-called credit are in the opposite direction. Credit is being withdrawn from the directly productive members of society and extended to financial middle-men. Moreover, there has been an increase of so-called public credit. The fact that States and municipalities waste the community's resources is lost to sight. Yet public loans are not pure credit to all. They are only partially voluntary. They are based, not upon productivity, but upon taxation. The credit of a community is thought to be inexhaustible because the power of taxation has not yet been seriously challenged. The spectacle of the present generation struggling under a growing burden of public debt is a gloomy one, but the prospect of the future is still more hopeless. We are purchasing a temporary relief at the expense of our children's

children.* Generations are to be born into economic slavery. Yet in spite of intensive taxation in the present and prospective taxation in the future, the capacity of the community voluntarily to create public debt has been exhausted almost the world over. Increase of such debt threatens to be on a coercive basis. Recourse has been had to forced loans in Continental Europe, the same has been threatened in Australia, while England is faced with the spectre of a huge debt which it cannot succeed in funding. The end is not in sight. The military conflict of 1914–18 is being followed by a financial repercussion throughout the world, with more disastrous results in human misery than the horrors of war.

The situation is the outcome of a refusal to recognise the elementary economic truth that a credit instrument must be free from all constraint. The kings in early days enforced their own cash currency. Whether good or bad, the king's coin had to be accepted. The result was that the kings took advantage of their position to cheat their subjects. Slowly they learned that depreciation of cash money led to national disaster. They were obliged to stop their malpractices. The path uphill proved harder than the path downhill. When Queen Elizabeth tried to restore the coinage debased

* The French Government in 1920 issued a loan at 5 per cent. repayable in 1980 at fr. 150 per fr. 100 nominal.

by Henry VIII. to its old value, it was found that the new coin disappeared from circulation as soon as minted. Sir Thomas Gresham, Master of the Mint, enunciated the so-called Gresham's law that bad money drives out good. Gresham was dealing, be it noted, not with a competitive, but with a State currency.* There is no evidence that under open competition bad money would oust good money. If money circulated on its own merits and not under State fiat, the better type would oust the worse, and the debased currency of the kings would not be accepted by their subjects.

The same law holds with regard to credit money. Under open competition the private bank-note, issued by reputable firms and based upon real wealth

* Gresham fully recognised this. The familiar form of Gresham's law that "bad money drives out good" is an incomplete version of the principle. Gresham saw clearly what subsequent economists have to a great extent overlooked, that the law only holds good of State-controlled money. The fuller statement of his principle is: "Where by legal enactment a government assigns the same nominal value to two or more forms of circulatory medium whose intrinsic values differ, payment will always, as far as possible, be made in that medium of which the cost of production is least, the more valuable medium tending to disappear from circulation."

An interesting corollary might be added to this, equally based upon the observed facts of modern industry, to the effect that where the State or other body decrees that different forms of labour shall receive the same pay, the less productive form of labour will oust the better form.

or constructive ability, has always competed successfully against State paper money, or against the notes of privileged banks, until suppressed by law. Under State control of finance, bad credit money drives out good credit money. It also drives out good cash money. Evidences of public debt circulate instead of credit instruments representing real wealth. Debased State paper has forced gold out of circulation. No country in Europe dare allow free traffic in gold. If it did so, its gold store would migrate outside its borders and its credit system would utterly break down. The countries of Europe have had to protect their gold stores by prohibiting the export of gold. These measures can have only temporary success, and do not operate with respect to fresh supplies of gold from the mines. The gold that is coming into the open market from the mines at the present time is being bought for the United States.

With the advent of paper money, power passed from the kings to the politicians. The latter have not yet learned the lesson that the kings were taught by their experience in debasing the coinage. Statesmen still think that coercive credit is better than free credit, that evidences of public debt are as good as evidences of real wealth or productive ability. They have suppressed the free note in favour of the privileged note. They have even

suppressed or limited the privileged note in favour of the State note.

Everywhere the result has been the same. Forced paper currency has always become debased. Whether it be the French assignat, the American green-back, the Soviet rouble, or the Treasury note, its value has fallen. Statesmen have multiplied evidences of public debt so enormously that the community can no longer absorb them. The money value of such evidences has everywhere fallen and the interest charges risen.

The banks have been obliged to take up huge proportions of public issues. The pressure exerted upon them by the State's hold on the central gold reserve left them no other course. The National Banks of England, France, Germany, Belgium, the United States of America, were obliged to support their respective States in a destructive war. The deposit banks were compelled to lend their aid to a vicious system of finance. Otherwise their cash resources would have been drained away as in the Napoleonic wars. The result has been to superimpose upon the circulating medium, the insufficient stock of gold, a huge superstructure of non-circulating or semi-circulating debt evidences which are straining the whole credit resources of the civilised world. If those gold stores could be maintained intact, industry might stagger fitfully

along, as it did in pre-war days. Under the centripetal system of finance, however, there is a constant tendency for the greater gold store to absorb the smaller. Gold in pre-war days had drifted from the local stores to the central national store, and had shown a tendency to drift further to the centre of the centripetal system, the north-eastern area of the United States. That process has been accelerated during the war. The interest due to America on the war debts is a yearly lien upon Europe's gold store. The issue of debased paper in England and on the Continent is a powerful factor which, under Gresham's law, will prevent inflow of gold.

One result of State control of credit can be foreseen. As gold migrates to America, it will become necessary further to restrict English credit, with the result either that English industry must dwindle or must be carried on to an increasing extent by the aid of American credit. The one-time mistress of the world's industry will find herself reduced to the rôle of a humble handmaiden, suing for favours from her powerful cousin.

What, then, is the essence of cash and credit finance? Simply this, that under a free system the most circulating form of commodity or credit will serve as money. But free circulation connotes value. A man will only accept freely what he

considers to have value, either in itself or in the result. Free credit means a note issue based on evidence of real wealth or productive ability. Under a coercive system, on the other hand, the worse form of cash money or credit will replace the better. Bad money or credit based upon evidences of public debt will oust value money or credit based on productive capacity.

Chapter Seven: *The Blight of Usury*

USURY is essentially a term of reproach. The usurer has been anathematised by the Church, punished by the State, denounced by the Moralist. The masses have risen in revolt against him and stoned him to death. Pogroms against usurers, especially when of Jewish blood, have been rife since the cash nexus infused itself into society. The end of the conflict has been extraordinary. The Church has ceased to curse, and is content to live upon its unearned revenues. The State has abandoned its efforts to punish, and is content to pay away millions of pounds each year to satisfy those who have lent it money. The Moralist is prepared to defend the system he once denounced. To him it is a stabilising and socialising factor. The masses, when not reduced to apathy, make sporadic attempts to burst the spell which binds them.

The change has been wrought by a simple artifice. Usury is a hateful idea. Usurers are rightly objects of moral scorn. But interest is an economic phenomenon and dividend-receivers are high in social esteem. Yet usury and interest are one and the same thing. Usury is payment for the use of some object. Interest is nothing more.

The most pervading factor of modern industrial-

ism is the dividend. Compared to it rent is a minor issue. Society contains more dividend-receivers than rent-lords. The total portion of annual produce paid to holders of stocks and shares is greater than that paid to holders of title-deeds. The problem has presented itself under many changing aspects, from the direct loan of gold by a petty money-lender to the formation of huge dividend-making concerns. Astounding as it may seem, the economists, after centuries of study, have produced no adequate explanation of interest.

To-day four different theories of interest hold the field. Not one of them commands respect.* Let us examine them briefly and then proceed to establish the true explanation.

The first theory is called the "productivity" theory. Its ablest exponent was Bastiat. Capital helps the labourer to greater production, therefore the man who supplies the capital is entitled to a share of the increased product. To clinch the argument Bastiat presents a concrete case. There are two carpenters, William and James. James makes a plane. William realises that he could make more planks by the aid of the plane. He therefore tries to borrow it. But, says James, "If I lend my plane I am deprived of its use, and you, who did not make

* Gide, p. 562: "What, then, is this value . . . represented by interest? . . . The question is by no means easy to answer."

it, will benefit. That is not fair." Obviously James is in the right. Nevertheless James is prepared to lend the plane for a just consideration. In a year it will be worn out, and of course he must receive a new one. Furthermore, he must receive a part of William's increased output—say a plank. So William borrows the plane on the understanding that he shall return at the end of a year a new plane and a plank.

At first sight the argument seems convincing. Reflection will show that it is not a statement of an economic principle at all, but merely a mental trick. Economics is a science of trends, not an exposition of a static fact. The position indicated above could not perpetuate itself, because it contains the very factors which would eliminate it from economic society. For if William recompense James for his old plane by making him a new one, then William has made a plane. Therefore there are two producers of planes in this microcosmic society, and only one consumer. The supply of planes will, therefore, outstrip the demand. They will become a drug in the market, and interest will not be paid for their use.

On another important point the argument is wrong. It is without foundation in economic history. No period can be shown where payment of interest for planes was made in planks. In more

general terms, no period is known where interest on one form of capital was paid in another form. When cattle were money, loans were made in cattle and interest was paid in cattle. When metal was money, loans were made in metal and interest paid in the same.

The second theory is the "use" theory. A man is prepared to pay rent for the use of a house, he is prepared to pay hire for the use of a horse. Why, then, should he not pay for the use of a capital? Again a mental trick, a presentation of one side of the shield. If the demand for houses is keen, rent will be paid. Suppose the supply exceeds the demand? Take a proprietor who does not desire to use his manor, and would let it to a tenant, save that no tenant is forthcoming. Then the reverse phenomenon will occur. The proprietor will receive nothing for the use of the house, but will even pay a caretaker to look after it. If a farmer requires not the services of his horse and everyone in the neighbourhood has sufficient horses, then the former will pay to keep his horse in idleness. He will even lend it gratis to keep it in trim.

So it is with money. Economic history teaches us that hoarding precedes lending. A man hoards his money because he has no present use for it. If another borrows it and repays it when the owner requires it, he is doing the owner a service, in that

he is saving him the risk and trouble of hoarding it.*

Gide's criticism† of the "use" theory of interest is interesting. "As the capital which is the object of a loan is nearly always circulating capital—as a rule, money—it is not a lasting possession like a house, but is destroyed in the very act of production. Coal thrown into the furnace disappears in smoke; raw material is transformed; money is spent in wages. How, then, can interest pay for the use of a thing, the characteristic of which is that it is consumed at its first use? . . .

"It is easy to reply that the capital lent is neither the coal nor the money, but the *value*. Now that is permanent, preserving its identity much better than a house, which sooner or later falls into ruins. . . .

* The reverse phenomenon to interest has been known to occur. A writer of a letter to *The Times* in October, 1845, states: "In Galway I was assured that so little do the people know of the value of money that they are constantly in the habit of pawning it. . . . A shopman said it was quite a common thing to have money pawned, and he produced a drawer containing a £10 Bank of Ireland note pawned six months ago for 10s., a 30s. National Bank note pawned six months ago for 10s., a 30s. Bank of Ireland note pawned six months ago for 1s., and a guinea in gold pawned for 15s. two months ago. The £10 note would produce 6s. 6d. interest in the year if put into the savings bank, while the owner, who pledged it for 10s., will have to pay 2s. 6d. a year for the 10s. and lose the interest on his £10."

† Gide, pp. 563-564.

The borrower may become the owner of the money and keep it as long as he likes, but he has not become owner of its value, since he must give it back in the form of other money." Gide therefore considers the "use" theory the best explanation of interest.

This seems a close approach to sophistry. Underlying it, however, there is an economic truth, which Gide does not clearly state. Capital in the form of a house is not the cause of interest: value is. But what is the permanence of value to which Gide refers? To speak of value preserving its identity, unless you can identify it, is meaningless. Value is not the value of a house, which may decline. It is not the value of the money, because the actual money lent may be used to buy a worthless house. What, then, is the identity of the value received by the borrower and returnable (with interest) to the lender? Surely it is none other than the call upon gold. The borrower loans a certain call upon gold, and he expects return in the form of a greater call upon gold. This point will become clear in dealing with the true cause of interest.

The third theory of interest is the "abstinence" theory, originated by Senior. Before capital can be used it must be saved. The man who saves it is doing a social service. He is abstaining from gratifying an immediate desire for the benefit of society, and his reward takes the shape of interest.

This explanation is entirely unsatisfactory, and has been abandoned. A mere refraining from an act is not a cause. Abstention is not an act of production. As Gide points out,* to refrain from eating eggs is not to produce chickens.

Moreover, the explanation does not square with economic life as a whole. The Indian ryot hoards without the stimulus of interest. The small dividend-receivers may indeed practise abstinence under the stimulus of gain, but the financial kings of the world have no need to do so. Their income increases faster than they can consume it. Lassalles' fine wealth of scorn destroyed for ever Senior's ingenious theory. "The profit of capital is the 'wage of abstinence.' Happy, even priceless expression! The ascetic millionaires of Europe: like Indian penitents or pillar saints they stand, on one leg, each on his column, with straining arm and pendulous body and pallid looks, holding a plate towards the people to collect the wages of their abstinence. In their midst, towering up above his fellows as head penitent and ascetic, the Baron Rothschild! This is the condition of Society! How could I ever so much misunderstand it!"

The fourth theory is the "time" theory. It is due to Boehm-Bawerck. The newest of all four, it is still held in certain respect. Interest is the price of

* Gide, p. 125.

time. Time is a factor in value. A hundred pounds down is worth more than a hundred pounds in the future. A dinner at once, as M. Gide instances,* is of more value than one to-morrow. If not, a dinner a hundred or a thousand years hence is as important as one to-day.

Here again we have only one side of the shield. A dinner to-day is valueless to a man who has already dined. A dinner to-morrow is an agony to a dyspeptic. Surplus dinners are a debit not an asset to a wise man. Surplus money is a burden. Yet interest originated, in the first place, from the use of surplus money. Money was hoarded because it might be more valuable to-morrow than to-day, next year than to-morrow. The horse sense of the community is closer to the truth than the erudition of Boehm-Bawerck.

Well may a celebrated modern exponent of economic science ask, at the end of all such explanations: "Is not our general preference for cash simply due to the fact that we know we have always the power to invest it at interest, so that we are really reasoning in a circle?"†

Let us reason in a straight line instead.

Usury or interest, both the Economists and the Socialists assert, is the fruit of capital. The system in which capital operates is called capitalism. What, then, is capital?

* Gide, p. 564.

† *Ibid.*, p. 565.

Immediately we are faced by an astounding fact that there has been a historic change in the definition of capital. In its earliest concept capital meant real wealth used in producing further real wealth. To-day it means paper claims (stocks and shares) to real wealth, or to debt, used in manufacturing further paper claims (dividend warrants and bonus shares) to the same.

Ricardo is definite.* "Capital is that part of the wealth of a country which is employed in production, and consists of food, clothing, tools, raw materials, machinery, etc., necessary to give effect to labour."

John Stuart Mill affirms the same thing.† "Whatever things are destined to supply productive labour with the shelter, protection, tools, and material which the work requires, and to feed and otherwise maintain the labourer during the process, are capital."

So far there is no doubt about it. Capital is material, the sum of those things which are used to produce further material wealth. Paper claims have not entered into the concept.

Henry George‡ excludes all paper claims from the category of capital. "Though all capital is

* Ricardo, *Principles of Political Economy*, chapter v.

† J. S. Mill, *Principles of Political Economy*, Book I., chapter ii.

‡ H. George, Book I., chapter ii.

wealth, all wealth is not capital." "Many things are commonly spoken of as wealth which . . . cannot be considered as wealth at all. Such things have an exchange value . . . but they are not truly wealth, inasmuch as their increase or decrease does not affect the sum of wealth. Such are bonds, mortgages, promissory notes, bank bills, or other stipulations for the transfer of wealth." If paper claims are not wealth, still less are they capital.

Karl Marx* makes capital originate with money. "The circulation of commodities is the starting-point of capital. . . ." "If we . . . consider only the economic forms produced by this process of circulation we find its final result to be money: this final product of the circulation of commodities is the first form in which capital appears."

Real wealth is fading from the concept of capital, and money forms are usurping its place. The capital which acquires interest is no longer real wealth, but a metallic or paper claim to wealth.

Gide says: "The capital which is the object of a loan is nearly always circulating capital—as a rule, money."†

Later on we find that metallic money drops into the background. The producer of interest is the paper claim.

* Karl Marx, Part II., chapter iv., p. 123.

† Gide, p. 563.

Gide finds* that "in everyday language, capital does not mean the instrument of production, but *all wealth which brings in a revenue to its possessor independently of his labour.*" But the wealth is not real wealth at all, as the writer goes on to state. "Long after the capital lent has been squandered in riotous living, or blown away in smoke on the battle-fields, it will still remain as lucrative capital—*i.e.*, as a credit claim in the hands of the money-lender or the fundholder.†

The wand of the economist has succeeded in transforming capital by gradual stages from material wealth to paper claims. A wonderful metamorphosis indeed. Is this truth or illusion, the white light of science or the black art of wizardry? The steam-engine, as capital, can draw a train. As capital, says the economist, the steam-engine can draw interest. The paper bond, under the deft handling of the economist, shares one function of capital, that of drawing interest. What a pity the economists are not clever enough to make it draw a train.

The Socialist school sidesteps the difficulty. It will not commit itself by saying what Capital is, but defines it by what it does. Capital, it says, is that which produces Interest. This is indeed a vicious circle. What is Interest? Interest is the

* Gide, p. 115.

† *Ibid.*, p. 122.

fruit of Capital. What, then, is Capital? Capital is that which produces Interest.

The economists see the absurdity of the Socialist position. Gide says:* "It is certain that the rôle of capital has changed with economic evolution; from a simple instrument of production, it has become an instrument of gain. It is no longer an aid to labour; it commands labour. It is this new social régime which Socialists call *Capitalism*. The fact that no wealth can be produced without the aid of some other pre-existing wealth, is an economic law the importance of which cannot be exaggerated. . . . We must give some name to this pre-existing wealth. Now the name we give it is *Capital*. If Socialists will not accept this name, let them propose another."

There is another and easier alternative. Let us continue to call Capital by its name—Capital, and let us give the proper name to that which obtains interest.

Capital is real wealth used in production of further wealth. Concretely it includes tools, machinery, engineering works, materials of every description.†

Finance is the claim or call upon wealth used to exchange present or future wealth. In our present system it includes gold, token claims to gold (*i.e.*,

* Gide, p. 116. † See Gide, p. 124.

silver, copper, nickel), and paper claims to gold. Paper claims to gold may be of fixed or varying gold values—*i.e.*, bank-notes and cheques, or bonds, stocks, shares, mortgages.

Production of wealth is a different thing to exchange of wealth. A machine is capital because it is used to produce. A gold coin is finance because it is used to exchange. The one operates upon commodities, the other upon ownership. A mine shaft is capital, because it aids in raising the ore to the surface. A railway is capital because it brings the produce to the market. The coin, the bill, the note do not operate upon the product in the same way at all. They alter neither its form nor its position. They transfer its ownership.

Capital and Finance are two inseparable factors in an economic society where the consumer of a commodity is not the producer. Though inseparable, they are not identical. The Siamese twins were joined, but they were two identities.

The whole of the science of economy has been befogged by the failure to recognise the clear-cut distinction between Capital and Finance. The province of Capital is production, that of Finance is exchange. The simplest tool of the primitive hand-workers is as much capital as the mightiest machine used in industry. The cowrie shell of the Pacific islanders is as much finance as the biggest

paper bond of a financial pool. Tools and machines assist labour to alter the form or the position of wealth; they do not change its ownership. Cowrie shells and bonds do not, and cannot, alter the form or the position of wealth, they but serve to transfer the ownership.

Let us apply this concept to the social problem. The Marxian doctrinaire says that the labourer is exploited by capitalism. He does not define capitalism, because he has no clear idea of what he means by capital. He does not know whether he means the machine or the paper bond. To him it is all capital. One might as well confuse a house with the mortgage on a house, and imagine that the sleeping accommodation of a city could be doubled by mortgaging all the houses!

The Marxian doctrinaire is not incorrect on one point, that the labourer does not get a proper return for his labour. The wealth of the world goes in greater degree to the non-producer than to the producer. Where, then, does the exploitation occur? Does it occur in production or in exchange? Is there some ghoulish property in the machines which the labourers use, that they filch from their users a part of the produce in the making? If so, Capital can rightly be regarded as an exploiter of the labourer. But economics in that case will have to be written in the language of the *Arabian Nights.*

In addition to the genii of the ring and of the lamp, we must admit those of the hammer and the crane, of the steam-engine and the loom, all evil genii filching a part of the labourer's product.

But there is the simpler explanation that the labourer is exploited, not in production, but in exchange. He works for a wage, for a financial consideration. The value of the financial consideration that he receives for his product is less than the value of his product. The reason is obvious. To provide capital for the labourer, to build him the factories and the machines which should improve his lot, finance is necessary. The financiers who provide that finance exact an undue toll in the form of dividend. To provide the labourer with his raw material, credit is necessary, and the financiers who provide that credit also exact an undue toll for it in the form of interest. The problem of exploitation can be reduced to a simple equation, with the minor factors such as rent omitted:

Full product of labourer = Finance of shareholder (dividend) + Finance of credit agent (interest) + Finance of labourer (wage).

Having made clear this fundamental distinction between Finance and Capital, let us proceed to ascertain the true cause of interest. Finance is

either coin or credit. Credit, in existing society, is the call upon gold. Gold owes its position to the fact that it is the most exchangeable or circulating commodity. In exchange it has an advantage over all other commodities.* This advantage is not a transient or accidental one: it is inherent and permanent. Moreover, since the exchange of commodities is an increasing factor in an industrial society, the most exchangeable commodity must obtain an increasing advantage over the less exchangeable ones. This advantage must find expression in economic relations. How does it do so?

It cannot do so in value or price. The price of a commodity is determined at long last, and ignoring transient fluctuations in supply and demand, by the cost of producing a similar article. Suppose, for example, that 1 oz. of gold costs as much to produce as 10 yards of cloth or 1 cwt. of mutton. Then these things will normally be equal in exchange and the equation will be:

1 oz. gold = 10 yards cloth = 1 cwt. mutton.

But the owner of the gold can always buy cloth or mutton. Anyone with coin in his pocket can walk into a shop and get what he wants. This is not erudite economy, but a simple fact of life. On the

* Gide, p. 289: "The possessor of money is in a much better position than the possessor of goods."

other hand, the cloth producer cannot always sell, neither can the butcher. The possessor of gold has therefore the advantage over the possessor of goods. He can exchange gold for goods at will, or he can defer his purchase. If, however, all gold possessors deferred their purchases, the butchers, clothiers, bakers, and farmers would be ruined. Some inducement must be offered to the possessor of gold, who is in a position to defer parting with his gold, to part with it temporarily, at any rate, to keep industry going.

This inducement may be in the form of increasing the value of gold. Suppose the clothier and the butcher lower the price of their stocks to one-half. Then the equation is:

1 oz. gold = 20 yards cloth = 2 cwt. mutton.

Now the possessor of gold can purchase double quantities whenever he likes. But he still has the most exchangeable commodity. Why should he buy? Why not withhold until he really desires the commodities which he can purchase at any time?

How, then, can he be induced to part with his gold? Obviously by offering him a consideration for its temporary use. That consideration is interest.

Interest, then, is the economic expression of the superiority of gold in exchange.

It follows that interest is not a function of capital at all, but a function of finance. It is a toll levied, not on production, but on exchange.

This may not be in accordance with the teachings of economists, but it is in accord with the facts of economics.

Let us follow the question further. If interest is a function of capital, then, by the process of supply and demand, the rate of interest will rise as the demand for capital rises, and will fall as the supply of capital increases. If interest is a function of finance, the rate will rise as the demand for money rises, and fall as the supply of money increases. In the first case the supply of and demand for capital will govern interest, in the second the supply of and demand for money will do so.

If the supply of and demand for money does not reflect itself in the rate of interest, it must do so in prices. This supposition is favoured by the economists, and to support it they have invented the Quantity Theory of Money, according to which price varies directly in proportion to the quantity of money in the market. This, like other economic theories, not being based upon observed fact, but upon preconceived notions, is wrong.* The Cali-

* Gide, p. 232: "This formula, known as the 'Quantity Theory of Money,' the discovery of which constituted one of Ricardo's claims to fame, is much discredited to-day."

fornian gold discoveries of 1849 caused a great influx of gold into England. There was no proportional increase of price, but enterprise was greatly stimulated.* The American Civil War and the issue of inconvertible paper notes forced gold to England. No increase of prices occurred,† but interest fell and industry throve. Circulating medium was plentiful and so commanded a less rate of interest. The tradesmen and the community benefited.‡

The value of gold, as stated above, is determined, like all values, by the cost of reproducing the commodity. If mining improves, the value of gold will tend to fall, because more gold can be produced per hour. The discovery of the rich Rand mines led to a lowering of gold value, and a consequent increase in prices, because gold, as a commodity, was easier

* Conant, p. 637: "Prices did not advance in proportion to the increase in the volume of metallic money . . . but enterprises of all kinds received a stimulus unheard of in the history of the world."

† Jevons, *Investigations in Currency and Finance:* "Ten per cent. may be taken as the best approximation which we can get to the rise in prices between 1845–50 and 1860–62."

‡ Horn, J. E., *La Liberté des Banques*, Paris, 1866: "In those arrondissements where formerly the bill was a myth and the gold louis a phenomenon, hundreds of thousands of francs, and even millions in specie and in bills, are now in continuous rotation, promoting a movement of transactions which grow in intensity and extent day by day."

to obtain. On the other hand, the great output led to an increased supply of the circulating medium. Hence the rate of interest fell. The average yearly gold output between 1870 and 1889 was some £M22. Between 1890 and 1902 the average was £M44. The result was an immense drop in the rate of interest. Consols at $2\frac{3}{4}$ per cent. were quoted at 97 in 1893 and 114 in 1896. Since that date there has been a growing call upon gold. States and communities have heaped up their public debt. The periodic payment of interest means a periodic call upon gold. Interest rates have risen until States to-day have to pay 7 to 9 per cent. Still more unfortunately productive concerns have to pay 9 to 10 per cent. Industry is forced to close down, and the spectre of unemployment haunts the world.

The economists tell us that interest is a function of capital. Does that in any way account for the rise in interest rates? The capital of England is in its mines, its plant, its motor transport, its factories. These were increasing prior to the war, and their increase should have meant a reduction in interest. Yet interest rates rose. Consols fell from 114 in 1896 to 91 in 1901. During the recent war Consols have fallen from 75 in 1914 to 45 in 1920. Was capital really destroyed to such an extent as to account for this fall? We started the war with

factories, ships, railways, lorries, mines, etc. Many of the ships were destroyed, but the railways, lorries, mines were not. What was destroyed was the product. Millions of tons of good steel went in shells and tanks, now lumbering the fair face of the world. The capital of England remained almost intact. Indeed, more factories were built, more ships constructed, lorries were completed in thousands. The war and its destruction stopped in 1918, but the bank rate rose to 7 per cent. in 1920. What, then, caused the rise in interest? Not destruction of capital, but inflation of finance.* Enormous public debts were created which represent claims

* The failure to distinguish between Capital and Finance leads to strange absurdities. Economists allege that the nation lived on its capital during the war, and will have to work harder in future to replace that capital. The *Economist* (April 2, 1921, p. 677), nevertheless, publishes the following statement of so-called

NEW CAPITAL APPLICATIONS.

1906	..	£M 120	1911	..	£M 192	1916	..	£M 585
1907	..	£M 124	1912	..	£M 211	1917	..	£M1,319
1908	..	£M 192	1913	..	£M 197	1918	..	£M1,393
1909	..	£M 182	1914	..	£M 513	1919	..	£M1,036
1910	..	£M 267	1915	..	£M 685	1920	..	£M 367

It will be seen that all through the war, although capital was being destroyed, new "capital" was created to a much greater extent than before the war. The fact is, of course, that capital (factories, rolling stock) was destroyed, but finance (paper calls on gold) was created, *and, with it, further interest charges.*

upon the gold store of the country. Those claims have to be met periodically, and to meet them puts a strain upon our credit resources by increasing the strain on gold. Hence trade credit is restricted, overdrafts are called in, and business men are asked to find employment where there is no prospect of selling their produce. The economists of the world meet in international conferences and speak of the need for further credits, while the bankers, by cutting down overdrafts, prove the need for reduced credits.

What does it mean, in actual fact? Nothing other than this, that the community is surfeited with bonds and debt-evidences of non-circulating nature, all of which have value ultimately because they represent, not real wealth, but varying calls upon gold.

This colossal mass of paper credit has been erected, not upon the capital of the country, but upon a meagre central stock of gold. It may be asked why the superstructure cannot be extended still further. If the various calls upon gold balance themselves automatically, why should not credit be still further extended, since it represents only paper transactions? One answer is not far to seek. The small trickle of gold from the gold stores of the various countries towards the centre of the system, America, has increased in volume. It has become a

stream and threatens to become a flood. Central Europe has been more or less denuded of the precious metal. Whither is it going? Largely, in the first place, to the vaults of the Federal Reserve Banks of the United States. But it does not stop there. The Americans are selling their paper titles to procure gold for their own needs, and the metal is going into the interior. That is one of the chief reasons why the English banking system is restricting credit, stifling industry, and increasing unemployment.

Capital, the economists tell us, is the source of interest. If a man makes with his own hands a small machine, that machine is capital. If he operates that machine and increases his product, the increase is the profit derived from capital. If, instead of making the machine, he borrows money to buy it, then the increased produce will be divided. Part will go to the owner of the machine, the capitalist, as profit, and part will go to the lender of the money, the financier, as interest. If the demand for money in the community increase, then the financier's share of the profit will increase. If the money scarcity becomes intense, the capitalist proper will have to part with almost the whole of the surplus produce to the financier. Does this happen? Let us appeal to economic history.

The limited liability company has ousted the private financier in almost all economic transactions.

The shareholder receives his part of the produce in dividends. Does the dividend represent interest or profit? The answer is that it combines both these items. One factor has swallowed up two shares of the surplus produce. The financier has obtained not only his own portion, but that of the capitalist. But what has happened to the capitalist? He has disappeared from the scene.* Very few men to-day manage and control their own machines. The capitalist of two generations ago has been reduced to a salaried manager. Centripetal finance has divorced the worker from his tools, and made him dependent upon a wage. It has divorced the capitalist from his capital and made him dependent upon a salary. The financier gets the reward of the increased productive ability of both classes.

Interest, the economist tells us, is a payment for the use of capital. The statement does not square with the plain facts of economics. Take the case of a capitalist. He owns a workshop, machines, materials, all forms of real capital. His capital is valued at £1,000 on a fair valuation. He has a friend, a financier, who has £1,000 in gold, or in a call upon gold. The equation is, therefore,

£1,000 in capital = £1,000 in gold.

* Macrosty, *Trusts and the State*, p. 131: "The typical capitalist of to-day is not the entrepreneur, but the shareholder."

Now the capitalist needs help from the financier. He wants credit. He offers to exchange, not capital for gold, but the call upon capital for the call upon gold. He gives the financier a mortgage upon his entire capital, value £1,000. The financier should give him, in return, a call upon his gold, value £1,000. Neither will realise the call upon the other's stock. The capitalist will draw cheques, and the cheques will be cancelled without the gold in the bank being disturbed. The financier will hold the mortgage and, upon repayment of the loan, will return it for cancellation, without the workshop, machines, etc., being disturbed. But experience shows that the equation is not

£1,000 capital=£1,000 gold.

For the call on £1,000 capital the financier will not lend the call on £1,000 gold. He will only lend the call on £750, if as much, and at a certain rate of interest. The equation is, probably,

Call on £1,000 capital plus £50 interest per annum=
Call on £750 gold.

In other words, so far from interest being a payment for the use of capital, it is a payment by capital for the use of the call upon gold. Interest may be the fruit of capital, but it is the financier who plucks the fruit.

Let us consider another aspect of the case. A

community possesses certain cash resources, sufficient to allow its products to be exchanged. Increased industry, clever invention, improved methods, double the output. How is the output to be exchanged? As already explained, either by increasing the cash resources, or by quickening their circulation, or by finding a substitute for cash. Normally all three ways will be tried. If the substitute for cash does not possess a great amount of circulating power it will be of little use. The community will, therefore, endeavour to get more cash resources. Failing that, it will accelerate the circulation. Movement, however, cannot be accelerated without stimulus. The stimulus must be found. One such stimulus is found by increasing the rate of interest. If interest rates are raised, endeavours will be made to pay debts more quickly. Overdrafts will be cleared more promptly, settlement of accounts pressed for, and cheques encashed sooner. The whole mechanism of exchange will be speeded up. But there are definite limits to such speeding up. Cheques must reach the clearing house for clearance, and the rate at which they can do so is limited by questions of transport, including postal delays. Equilibrium will in the end be established, but the point of equilibrium will not be the optimum. Those firms that can obtain credit at the higher rates will exchange their pro-

ducts. The others will go out of business. One important feature will be obvious. The financier will obtain a higher share of the profit.

What, then, is interest? It is the toll exacted from society by the holders of gold or the call upon gold, by virtue of the circulating advantage of the latter over all other forms of wealth.* The rate of interest varies, not with the capital of society, but

* The circulatory or exchange advantage of gold is, of course, not the same with respect to all commodities, some of which are more exchangeable than others. Hence we should expect the rate of interest to vary with the exchange factor of the commodity upon which the loan of gold, or of the call of gold, is advanced. This is actually the case. Land is naturally one of the least exchangeable commodities, from the simple fact that it cannot be transported to the market, but must be sold *in situ*. Hence the rate of interest in respect of loans on land is higher than that on marketable goods. The difference is so great that lending money or credit on land has ceased to be regarded as sound banking business.

The same feature is seen in the rate of discount for commercial bills. A three-month bill is more easily exchangeable than a six-month bill. It represents goods whose marketability in a short time is more probable. Hence the rate of discount on three-month bills is less than that on six-month bills, as a glance at the money columns of any newspaper will confirm.

Similarly the marketability or exchange factor of the security offered to banks as collateral influences the rate and conditions of interest. The bonds of a financial trust are steadier in value and more marketable than those of an industrial company. Hence banks will lend to the former on easier terms than to the latter, a factor which is aiding in the trustification of industry (see p. 215 for an instance of this).

with its financial needs and resources, and is one of the factors which determines the speed at which the call on gold circulates.

Analogies are, necessarily, imperfect. The following may serve to present the above idea concretely. Picture a country separated into two parts by an innavigable river. To the south of the river the ground is fertile and crops can be grown in plenty. To the north the ground is well mineralised and favourable for industry. The community is progressing. In time a bridge is thrown over the river. Interchange between the north and south banks leads to specialisation. Industries spring up in the north, agriculture develops in the south. The traffic over the bridge increases in volume. The owners levy a moderate toll upon it. In time the volume of traffic so grows that it congests the bridge. Industries are checked owing to inability to market the produce. The traffic over the bridge must be speeded up. The owners increase the toll and make it dependent upon the time the traffic takes to cross the bridge. Slow traffic must pay more than fast. The result is that the vehicles become faster and faster. The owners widen the bridge as much as possible so that it can take a greater volume. The excessive speed of vehicles causes a collision. Traffic is suspended, and both portions of the community are deprived of their

necessaries. Slowly the wreckage is cleared, and the traffic gradually gets into its stride again.

The above gives a graphic representation of modern economic society. The bridge is the gold basis upon which exchange is conducted. The toll for passage over the bridge is the interest paid by society for the call upon gold. Its rate varies with the speed of circulation. The breakdown is the financial crisis from which industry slowly recovers and speeds up until the inevitable breakdown again happens.

Chapter Eight: *The Mother Trust*

The industrial trust has attracted much attention in the lifetime of the present generation. Napoleon described England as a nation of shop-keepers. These shop-keepers, however, have been rudely disturbed. Their sleek prosperity has been challenged by the growth of the system of multiple shops. They find themselves in competition with powerful firms. Their sons can no longer hope to succeed to the business, because the latter is being absorbed daily by limited companies. The son's outlook is not that of an independent retailer, but of a dependent manager.

The trust movement in industry is the trump-card of the Socialist. Efficient or inefficient as collective control may be, it is inevitable, because the obvious end in sight is that every branch of industry will be centralised under one control. It is better for the community that the controlling body should be elected by the people than that it should be an arbitrary board of directors.

It is assumed that the trust movement is an inherent trend in what the Socialist loosely calls "the capitalist system". Half-hearted attempts are made to explain how it develops. Competition is alleged to be wasteful, and as competition can be

eliminated by combination, waste is lessened and efficiency is promoted. The trust is, therefore, industrially more efficient than the individual competing units. By extension of the same line of thought, the State will be still more efficient than a congeries of competing trusts.

Unfortunately for the logic of the argument, the conclusion reached is false. The State is notoriously inefficient in industry.*

It is certainly true that large concerns are more efficient than small ones in certain operations. A village smith cannot build a battleship, for example; on the other hand, he can shoe a horse better than an armament firm can. Certain factors are favourable to the centralisation of industry, others tell against it. In a free economic system equilibrium would be established. The present trust inflation is, however, in no sense a result of freedom, but of State restriction of finance.

The factors against centralisation are ignored in considering the industrial trust. Only those favouring centralisation are emphasised. Yet the former are probably more potent than the latter. A central factory may secure an advantage in actual manu-

* Gide and Rist, p. 447: "Even at the present moment one is tempted to ask whether this growing multiplicity of State function is not in danger of arousing on the part of consumers, entrepreneurs and workmen, a general feeling of contempt for the economic capacity of the State."

facturing processes, but its material will generally come from a longer distance, while its products have to be distributed over a greater area. The cost of carriage is therefore greater. Big concerns, again, never get the same amount of work out of their employees as do the small ones. It is well known that a workman prefers to work for a big company than for a private employer because he has an easier time. The limited liability system carries with it limited responsibility. A manager cannot show the zeal in furthering the interests of anonymous shareholders that he would in furthering his own. In a large concern routine is apt to choke efficiency, change of method is harder to introduce. Big trusts fail to meet the competition of brisk smaller concerns, and are frequently able to pay only small dividends.*

A study of the history of the industrial trust,

* President Wilson, p. 133: "Read the statistics of any trust. They are constantly nervous about competition, and they are constantly buying up new competitors in order to narrow the field. The United States Steel Corporation is gaining in its supremacy in the American market only with regard to the cruder manufactures of iron and steel, but wherever, as in the field of more advanced manufactures of iron and steel, it has important competitors, its portion of the product is not increasing but is decreasing, and its competitors, where they have a foothold, are often more efficient than it is."

P. 141: "The big trusts, the big combinations are the most wasteful, the most uneconomical, and, after they pass a certain size, the most inefficient way of conducting the industries of the country."

moreover, reveals one important fact. Its development has followed, not preceded, that of the financial trust. The earliest pronounced symptom of trustification in English industry can be placed between 1880–90,* though an underground tendency was at work before that date. In 1884 the shipping industry arrived at an agreement with regard to the division of the Chinese trade. Late in the nineties, coalescence of various companies into unions became manifest. In 1888 the Salt Union was formed; the Alkali Union followed in 1891. The combination of metal-bedstead manufacturers took place in 1893, followed shortly afterwards by dyeing and earthenware combines. The big English combines, such as Coats and Company in cotton thread, Armstrong, Whitworth in steel, date from 1895, and later. Vickers absorbed the Maxim-Nordenfelt concern in 1899. The industrial trust movement gathered pace slowly in England, but its acceleration has been increasing constantly. The Great War checked it for a time, as financial resources were diverted to a single aim, and the flow of public money called into existence many new firms. In the two years following the war (1919–20) trustification proceeded at a greater rate than ever before. The national phase of the movement is almost completed, and the international phase is in swing.

* See Macrosty, *Trusts and the State*.

The trust movement has been generally of three kinds. The earliest form was that of mere *aggregation*. A steel firm took over another steel firm, a colliery company absorbed another colliery company. A newspaper bought out its struggling rival. A later form is that known as *integration*. The tendency is no longer horizontal but perpendicular. Big concerns endeavour to buy out ancillary businesses, to secure the supply of raw material, or to control the channels of sale. The *Daily Mail* purchases paper mills, it then buys up forests to secure material for the latter. Guest Keen buy up collieries. Vickers buy out waggon companies. In the retail business the tendency is toward *congregation*. Big firms open into other branches of industry. The multiple shop system, in which each branch sells the same commodity, is challenged by the general store, in which almost every conceivable commodity, comprising every branch of retail trade, is to be obtained. Selfridge's, Harrod's, Whiteley's, come into prominence.

Important as is the trust development in British industry, the fact should not be lost sight of that it did not originate here, but came from the United States, the centre of centripetal finance. The first surface indication of the movement can be traced as far back as 1866, when amalgamations in the salt industry were effected.* The trade depression

* Ripley, p. 4.

during 1873–79 checked the new tendency, but from 1880 onwards its force became irresistible. Aggregation of small concerns into larger associations went on apace from 1880 to 1887. The trust became a growing menace, and its legality was challenged. But the law was impotent, and the legal character of the trust was acknowledged. In 1887 a new system emerged. The trust was no longer the entire absorption of one concern by another. Holding corporations were formed. These secured control, not of a concern in its entirety, but of sufficient shares to allow the holding corporation to determine the trade policy of the company. The most prominent of the earlier of such corporations was the United States Steel Corporation formed in 1901. In vain legal aid was invoked. The Sherman Anti-Trust Act of 1890 did not avail. Various States tried to cope with the difficulty by prohibiting "intercorporate stock-holding". They were met by other States who deliberately favoured such corporations in order to add to their revenues. The great call upon American output during the Great War has checked the tendency. The Amalgamated Copper Company dissolved into its various components in 1915. Other huge concerns showed a tendency to do the same, but there is no evidence that this is other than a transient effect of the flood of public money due to war conditions.

The growth of the trusts has been accompanied by most perturbing signs of increased commercial immorality and unsound business methods.* Their control has been characterised by excessive financing. Their management has been speculative and profit-snatching. They have enhanced prices in many cases. In others they have cut prices to the producer of raw materials. If they have spared the public, it has been to lessen the profits of the firms supplying them with their material, and so to obtain control of further industries. Their methods have been open to grave censure. They have indulged in boycotting and coercion, in market manipulation, and in secret rebates. They have squeezed out their rivals, instituted bogus competition, resorted to espionage. If they represent economic efficiency, then the science of economy is the antithesis of the science of morality, human knowledge is founded upon two directly antagonistic bases, and philosophy, which seeks to unify all knowledge, is the freak creation of a distorted mind. The old dilemma of Proudhon presents itself with renewed force.†

* Cp. Ripley, p. xxv.

† "It is surely a sad symptom for a science, when, in developing itself according to its own principles, it reaches its object just in time to be contradicted by another; as, for example, when the postulates of political economy are found to be opposed to those of morality, for I suppose morality is a science as well as political

It is difficult to understand how economic observers can have failed to notice that the industrial trust is not an inherent but entirely an artificial feature in economics.* To establish this fact it is only necessary to trace the history of the earliest, the greatest, and most pervading of all trusts, the banking trust.

Economic history shows clearly and distinctly that free development from the cash to the credit nexus is identical with the emergence of the note-issuing bank. In this process the symptoms of trustification are entirely absent. The tendency of note-issuing banks is centrifugal. They sprang up as independent organisations wherever the community's demand for credit justified their existence. In England their number was exaggerated by the six-partner restriction. In 1750 they were 12 only. In 1793 they numbered 400. In 1810 they reached the total of 721. The removal of the six-partner restriction in 1826 led to the flimsier banks succumbing before more stable institutions. Their place was gradually taken by large joint-stock banks. In 1842 their number was reduced to 311, and at

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economy. What, then, is human knowledge, if all its affirmations destroy each other, and on what shall we rely?"—Proudhon, *System of Economical Contradictions.*

* President Wilson, p. 130: "The trusts have not grown. They have been artificially created."

the time of Peel's Act (1844) they had fallen to 207, while 72 joint-stock banks had been formed.

In Scotland and Ireland, as will be seen later, the development of the note-issuing banks took place under conditions of greater freedom. The growth was more steady and constant, and lacked the over-hasty and impromptu aspect that the Bank of England's monopoly forced upon English banking.

Peel's Act prevented the formation of new note-issuing banks. It not only checked the current, it turned it in the reverse direction. From that day onward the tendency to trustification in finance has been evident. New banks have been increasingly difficult to found,* while old banks have been more and more easily absorbed. In Jevons' time there were some 267 private and 121 joint-stock banks in England and Wales.† In 1880 their number had fallen to some 300. Centralisation has progressed at greater and greater speed. Early this century the number had fallen to fifty. The Great War checked the movement somewhat. In 1916 there

* Bagehot, p. 88: "To collect a great mass of deposits with the same banker, a large number of persons must agree to do something. To establish a note circulation, a large body of persons need only *do nothing*. They receive the banker's notes in the common course of their business, and they have only *not* to take those notes to the banker for payment. If the public refrain from taking trouble, a paper circulation is immediately in existence."

† Jevons, *Money*, p. 320.

were no banking fusions. In 1917 there were five. In 1918 there were eleven. In 1919 there were ten. To-day there are only five big banks and nine smaller banks.* The five big banks between them control nine-tenths of the business of the country.†

Of the old English note-issuing banks, apart from the Bank of England, not one remains. The Bank of England itself has practically ceased to function as a bank proper, and has become merely a banker's bank.

The trust movement in banking preceded that in industry by more than a decade. In 1865 Lloyd's Bank was founded by the fusion of two banks in Birmingham and one in Wednesbury. Before 1890 twelve other banks had been absorbed. Between 1890 and 1900 fourteen further absorptions had been made. Between 1900 and 1910 the number was increased by thirteen, four of which were banks which had already absorbed many others previously. Between 1910 and 1914 three more banks joined the combine. In 1918 the combine acquired the Capital and Counties Bank, which had since 1883 itself swallowed up some twenty-five other banks. The same year (1918) showed a further development of the centripetal system in the absorption of banks

* Excluding Coutts and Co., which has been absorbed by the National Provincial and Union.

† Negotiations are believed to be in progress for the amalgamation of two of the Big Five banks. See *Financier*, November 24, 1920.

doing business outside England, Lloyd's acquiring the London and River Plate and the National Bank of Scotland. In 1919 the West Yorkshire Bank, Limited, was acquired.

In the same year as the Lloyd's combine, Parr's Bank started on its career of fusion. In 1865 Parr and Company, of Warrington and St. Helen's (founded 1788), became Parr's Banking Company. In 1878 it absorbed Dixon and Company of Chester, in 1883 the National Bank of Liverpool, in 1892 the Alliance Bank. In 1894 three more banks came into its orbit, and in 1896 it became known as Parr's Bank. From 1896 to 1909 it absorbed nine other banks, of which Stuckey's Banking Company represented the combination of fourteen separate banking houses. Parr's Bank has, in turn, followed the fateful trend, and has been swallowed up by the London County, Westminster and Parr's Bank.

Among the five big banks there are working understandings and agreements. The Baring smash led to the formation of a Banking Committee, representing the big joint-stock banks, which meets regularly to determine general policy. The Big Five have also joint interests in certain colonial banks,* and the tendency to fusion is still working to produce one single trust in all British banking.

* *E.g.*, Lloyd's Bank and the National Provincial and Union Bank are joint proprietors of Lloyd's and National Provincial Foreign Bank, Ltd.

The same process has been going on in the United States. The National banks founded during the civil war have become more and more interlocked. Within three years of the formation of the National banks the first indication of an industrial trust can be traced (1866). It is not necessary, therefore, to seek in economic theory an inherent tendency towards industrial trustification when an easier explanation strikes the eye in the creation of an unnatural banking ring.

It has already been pointed out that the old note-issuing country banks were the stimulators of the spirit of enterprise that enabled England to make its extraordinary forward bound at the beginning of the industrial era. When note issue was stopped banks ceased to promote enterprise. Any such step was not consonant with the artificial form of cheque-overdraft banking. Agriculture ceased to be a banking investment in the middle of the last century. Some of the old private banks, indeed, endeavoured to remain true to their principles. A modern writer* finds it curious that Greenway's Bank, of Warwick and Leamington, which failed in 1887, had been financing railways and had found the money to run a tannery. Is it, then, such a crime to promote industry? Is it really bad banking, or is it not perhaps the unnatural banking system that is bad?

* Powell, p. 667.

The stoppage of note issue led, as we have seen, to the cheque-overdraft system, to the formation of limited companies, the financial trusts, and the financial pools.

In these four phases of centripetal finance is to be found the whole solution of the trust tendency in industry.

The cheque-overdraft system favours old-established industries at the expense of new ones. Old-established firms can get credit when new firms ask in vain. In case of stringency the credits are first withdrawn from the latter. When the Great War ceased there were several firms building air-machines in England. To-day the smaller ones have dropped out for want of credit facilities, while Vickers, not originally an aviation firm at all, still carries on. This crushing out of new firms in time of stringency is the lesser evil. The greater one is that in normal times the new firm finds it extraordinarily difficult to start at all. In a new branch of industry, such as aviation, where an unknown field is open, new firms may spring up, but in an old branch of industry it is practically impossible. The existence of new firms is an outstanding obstacle in the way of trust formation. In the earliest days of the trust movement, when the Saginaw and Bay Salt Company tried to absorb the Ohio River Association, they failed in their first attempt because the latter was unable

to control some new works at Pomeroy which refused to join the combine.*

The second step towards trusts is supplied by the limited company. The old private banker knew intimately the possibilities of the businesses he financed. A rising, capable business man could get more credit from him than an older, less enterprising firm. The private banker was a specialist in judging business capacity. The shareholder of to-day is not a specialist at all. He is just an ordinary person with a small call upon gold. Not being in the position to judge of business capacity, he is attracted by size, by acquired reputation. If a big firm wishes to increase its finances, it is certain to meet with a response from the investing public. If a small firm wishes to do the same, the issue is very doubtful. The result is obvious. The big firm can always raise the money to buy out or freeze out its competitor.

The third step is supplied by the financial trusts. These bodies buy for control. They obtain sufficient shares in an industrial company to get the appointment of the directors in their hands. They then absorb the company. Their influence upon the Stock Exchange is such that they can unduly deflate or inflate the price of industrial shares. They are therefore in a position to buy at their

* Ripley, p. 11.

own price, and they take advantage of this position.*

An interesting example of how the financial system works is shown by the recent history of the Dunlop Company. Long ago the inventor of the pneumatic tyre was bought out by the financial workings of the limited company system. After the war the limited company, beguiled by the then favourable prospects, entered upon a policy of expansion, and undertook big commitments with respect to buildings in America and stocks of tyres in England. The marked credit stringency of the latter part of 1920 found it in an unfavourable position, and it had difficulty in procuring the means to carry on. It sought aid from a financial trust (the British, Foreign and Colonial Corporation, Limited), which was thereby enabled to appoint as chairman of the company one of its own directors. At the meeting of February 11, 1921,† he stated: "The company was in the throes of a domestic crisis, which, though only part of a world crisis, was none the less severe. . . . I then approached my ex-

* Powell (p. 472) points out that the earlier financial trust rarely changed its investments. Now, however, the trust "is becoming less a means of vicarious investment than a recognised necessary factor of the modern Money Power, taking its share in the guidance of the policy of the great financial hierarchy which now controls the economic destinies of the world."

† Report in *The Times*, February 12, 1921.

cellent friends, the London Joint City and Midland Bank and Lloyd's Bank (who are the bankers to the British, Foreign and Colonial Corporation, Limited), for the provision of the necessary credits, and I want to pay public tribute to the splendid spirit shown by these great institutions when they realised the true facts of the situation. I was asked to prepare an exhaustive report on the financial position of the Dunlop Company, and each bank has satisfied itself of the accuracy of my statements through their own accountants, and the credits asked for were granted."

Without wishing to indulge in carping criticism, one can only reflect that the public spirit of the big banks shows itself more markedly in their dealings with their "very good friends" of the financial trusts than with the industrial company. Apparently the Dunlop Company was in a sound position, but the banks would not give it the necessary help except through the agency of the financial trust. So under the present system control passes from the inventor to the limited company, and from the limited company to the financial trust. The old free system of note-issuing banks favoured the inventor. The modern system leaves the inventor derelict and fosters the financial trust.

The fourth step is supplied by the financial pools.*

* Ripley, p. xiii: "*The pool* is probably the oldest, the most common, and at the same time the most popular, mode of obviating the evils of competition."

These pools have not reached their full development in England, and their actions have not yet been the subject of searching enquiry. In America we find that they not only control industrial companies, but also the banking system. The inner history of the Copper Pool, which operated just prior to the financial crisis of 1907, is very instructive. A pool of minor financiers was formed which endeavoured to inflate the value of copper shares. It became heavily committed in its dealings, and in order to secure its hold on the market it used the pooled resources to control credit institutions. It secured domination of several banks in this way.* It forced up the price of copper shares. Then, suddenly, the market gave way. Selling copper orders were poured in from all quarters. A sudden restriction of credit occurred. The collapse in the stock market was the most sudden and violent Wall Street had ever known. The pool was broken, and it dragged down with it its dependent banks.

* "Mr. Morse first, then the Thomases and the Heinzes, had, after securing one bank, hypothecated the stock of that bank in various financial institutions . . . all over the country, had taken the money obtained by a loan on the stock in one bank to buy stock in another, had mortgaged that and bought into still another, and so on . . . after securing control of banks, they had made loans to themselves for the flotation of promotion schemes, and for the conduct of operations in the stock market." Lawrence Dunning, "In the Days of the Panic," in *Van Norden Magazine*, December, 1907.

The Mercantile National Bank, the National Bank of North America, the New Amsterdam National Bank, and other institutions were unable to meet their calls. On October 21, 1907, the celebrated Knickerbocker Trust Company had to seek aid to enable it to weather the storm. That aid was withdrawn, and its clearing bank refused to clear for it. Next day the Knickerbocker Trust suspended payment with deposits of $M60.

The copper pool was broken. The social student might see in such an event a ground for elation. There is none. The copper pool was not broken by the workings of just retribution, by the moral forces of the community. It was smashed by the machinations of a still greater pool. J. P. Morgan was not the man to allow any rivals near the throne. The banking system of America was his special preserve, and the smaller operators were to be taught a sharp lesson. The affair enabled him to get complete and recognised control of the whole system.*

To-day the Morgan pool dominates not only America but, directly or indirectly, wholly or in part, the industrial life of the world. Its credit manipulations are forcing German firms to sell out to French and English firms, and French and English firms to make working agreements with American firms. The United States Treasury is not its only

* See p. 138.

servant. The actions of the politicians of Europe, consciously or subconsciously, willingly or unwillingly, are subject to its thraldom. The statesmen of the world, large as they loom in public estimation, are but as clay in the hands of influences they cannot control, because the control is in the hands of the all-powerful Morgan pool.

Here, then, is the answer to the Socialist and the economist. Industrial trustification is not an inherent vice, a legacy of original sin due to fair competition in the economic system.* It is not a normal state of a healthy and developing body, but a festering ulceration produced by a state-restricted credit system. The four steps are complete. Prohibition of free note-issuing banks limits fresh enterprise. Limited companies favour large concerns. Financial trusts obtain control of the large concerns, and pools manipulate the trusts. At the same time, the centripetal system lures from the individual his meagre cash store. The branch bank hands it over to the head bank, the head bank places it in the central bank. The original depositor is lulled into inertia, or by issue of forced paper currency legally prevented from getting back his

* Ida M. Tarbell, *History of the Standard Oil Company*, vol. ii., p. 288: "Mr. Rockefeller has systematically played with loaded dice, and it is doubtful if there has ever been a time since 1872 when he has run a race with a competitor and started fair."

gold. His call upon his deposit is for practical purposes inoperative. On the other hand, the central store of gold in every nation is at the mercy of the pool interests. The banks themselves dare not refuse to obey the directions they receive. The pools have the effective call upon gold, and by use of that call they obtain control of industry. The industrial trust is an effect of their operations.

On the one hand, the expansion of industry and the specialisation of function combine to create a need for greater credit facilities. On the other, the control of such facilities passes into fewer and fewer hands. Permanent credit stringency is the result. First agriculture declines, then small tradesmen tend to disappear, then the smaller companies are forced to unite with larger ones, and finally the larger ones are compelled to combine.

Here is found an explanation of a change in the nature of trustification for which the economists appear to have found no solution. Aggregation is giving place to integration. If, however, trustification were due to the greater efficiency of the large concerns, aggregation would remain the normal mode. An efficient newspaper company would naturally absorb an inefficient smaller rival. A steel factory would swallow up its competitor. The directors, knowing their own industry, would confine their abilities to that alone. But the modern

newspaper buys up its paper mills and then its forests. The steel company buys coal-mines and waggon companies. What is the explanation of this untoward development? It is simply this, that in a system that is characterised by credit stringency development will tend to shape itself along those lines that will relieve the stringency. If two newspapers each spend £M1 per annum upon paper, they must use up part of their credit resources in doing so. If one of them absorbs the other, and the combined circulation remains the same, there is little, if any, relief in the strain on the total credit resources of the combined firms. But if one newspaper uses its resources, not to buy out its rival, but to buy out the paper mill that supplies the £M1 of paper, a considerable relief is effected. Before the combine the paper mill was perhaps using credit resources of some £800,000 per annum in buying raw material, and the newspaper some £M1 of credit resources in buying paper. The total strain involved thereby is £M1·8. If, however, the newspaper buys up the mill, there is no longer any need for a credit transaction to cover the purchase of the paper from the mill. This becomes merely a matter of internal book-keeping in the books of the combine. The strain upon credit is relieved to the extent of £M1, more than 50 per cent. of the whole.

That the saving of credit resources is a potent factor in integration can be seen from a recent case. In December, 1920, Baldwins bought out the British Mannesman Tube Company. The chairman of the latter company explained at the general meeting why the directors had been compelled to accept Baldwins' offer against the wishes of many of the shareholders. He said:* "At the present moment we have a large proportion of our capital locked up in carrying supplies of steel which we are bound to hold—whether on a falling or rising market—to ensure the constant working of our mills and the protection of contracts we have entered into. If this arrangement goes through we shall be released from this burden. Our arrangement with Baldwins will provide for a steady supply of steel at competitive prices. . . . The money released by reduction of stocks of raw material will enable us to lay down further mills at Newport and to carry through much needed betterments at Landore, and thus reduce costs of production, and be in a better position to compete on equal terms in the world market with those concerns who already enjoy the advantages of allied supplies of raw material."

Integration, then, is merely a method of conserving cash or credit resources in order to apply them

* Report in *The Times*, December 22, 1920: By "capital" the chairman means, of course, finance or credit resources.

where they are most urgently needed. It naturally is much in evidence in an industrial society upon which bad laws have inflicted a chronic credit stringency.

Integration is not a phenomenon associated with trusts alone. It has its place in the life of the humblest individual. If a man has sufficient cash or credit resources, he will pay to have his linen washed, he will dine out at restaurants, have his boots polished by a boot-black. In short, he will obtain services from individuals upon a money basis. If he is short of money he will wash his own linen, cook his own food, or get his wife to do so, polish his own boots. He will conserve his cash for those operations where it is indispensable. He is integrating industry as much as the most powerful corporation in the country. He is reversing economic development; he is substituting generalised for specialised industry, as is also the trust movement. Both are cases of economic involution, not of evolution.

The tendency to trustification is, then, no natural phenomenon, but is induced by the centripetal system of finance. Indeed, in spite of the artificial tendency so created, signs are not wanting that industry girds at the restraint and would gladly escape. Every loosening of credit restrictions, local and temporary as it may be, is the signal for

the springing-up of new firms full of enterprise and the competitive spirit. The outpour of public credit during the war, artificial as it was, stimulated not by normal considerations but by the will to overcome a pressing peril, led to the creation of many new businesses. Aeroplane firms, for example, multiplied. Handley Page, Martinsyde, Short, and Sopwith all produced machines of great merit, showing originality in design and enterprise in construction. The post-war restriction of credit, the increased rate of interest, the smaller margin of profit, has combined to restrict their operations. Their more powerful rivals, with less efficiency but with greater financial resources, are weathering the storm better than could the smaller firms.

Not war conditions alone, but normal peace conditions testify to the keen desire of industry to escape from trust domination. No industrial trust has succeeded in dominating the entire output of an industry. The strongest have been worsted in the conflict. The Standard Oil Corporation could not freeze out the Royal Dutch Company. The United States Steel Corporation has met with fierce competition from its rivals. Shipbuilding is still the field of competing companies. Lyons has not been able to eliminate the smaller catering firms. The tobacco combine has equally failed. Selfridge's, Harrod's, the great American department

stores, the whole clan of *congregated* industries have not succeeded in eliminating the specialised shop.

In new industries the natural anti-trust tendency is still more marked.* Numerous cycle, motor, rubber companies have arisen within the last few years. Motor-traction companies abound all over the country-side. Gramophone and autopiano companies sprang up in many quarters. In agriculture the broad acres of America cannot vanquish the small English farm or the *petite culture* of the Continent. The virility and the independence of industry was never more marked. Yet over all the superabundant energy of the industrial world lies the deadening pall of financial domination.

The explanation of the centralising trend is not to be sought in commerce but in finance. The world has sought in vain relief from the cash nexus. Machines do not attract to themselves other machines. Factories bear no interest in the shape of other factories. Gold, by virtue of its circulating power, does possess the power of attracting other gold. Cash bears interest in the form of cash. The call upon gold carries with it an annual increment, a yearly tribute to the centripetal power. A hundred pounds invested by Adam would have centralised the gold resources and industrial wealth of the world. Even at 2 per cent. it would have amassed unto

* Compare Gide and Rist, p. 475.

itself the entire production of the human race—the yearly toll of interest would have exceeded the total annual output. Adam knew not the value of gold. His descendants learned it slowly. The process was deferred for many generations, but to-day it is in full swing. The community groans under the toll exacted by the financier. Enterprise, invention, determination, labour, all are powerless to cope with the increasing grip of the financial octopus. Millions are born to spend long lives of toil with diminishing hope of escape. The spread of education, the growth of moral and social ideals, avails them not. Science may work wonders and philosophy open up fresh vistas, but the product of the toil of their hands and of their brains passes unerringly into the possession of the financial kings.

The financial system is the mother trust.* Once that system is reversed, the inflated industrial concerns will perish. The economic organism is suffering from an unnatural elephantiasis which a return to freedom in finance will cure. The disease will pass when the cause is removed.

* President Wilson, p. 146: "This money trust, or, as it should more properly be called, the credit trust . . . is no myth, it is no imaginary thing."

Chapter Nine: *A Glimpse of Freedom*

THE history of economy is a tale of discarded theories. Each of these theories has seemed good in their time, has controlled thought for a period, and then has passed for ever. The era of its domination has been short. The Physiocrats and the Bullionists have had their day. The wage-fund theory, the population theory, the quantity theory of money, the Single Tax of Henry George have lost their sway. The theories of Interest have never commanded universal respect, and, as has been shown, are erroneous. Protection and Free Trade have fought a battle royal for a century. At one time the Free Trade theory threatened to win outright. Now the drift is markedly in the opposite direction.

One theory has compelled homage from a greater section of adherents for a longer period of time than all other theories. Its application is world-wide, and has been so for more than a century. It is the theory of State control of note issue. This theory, like the others, had its origin in experience over a limited range of economic facts. Like the others, it will die only when it is clear that it no longer squares with our increased economic knowledge.

The limited experience of English banking over

a period of 150 years, from 1694 to 1844, in a partially industrialised community, had apparently taught that note issue was a vice, intolerable if unchecked, tolerable only if rigidly controlled. The economists have accepted the doctrine as sacrosanct, and have surrounded it with a ritual of arguments.

Briefly, the arguments are as follows: If freedom of note issue is allowed, an undue number of persons or institutions will avail themselves of it, they will issue an undue number of notes, the issue will cause an undue inflation of credit, which will lead to an undue frequency of financial panics. In addition, the control of credit will tend to drift into the hands of discreditable persons, whose aim will be to enrich themselves rather than to help to build up industry.

As stated above, the doctrine was based upon a limited experience of English finance. True it is that England was the most advanced, industrially and financially, of all countries; exceptional weight was therefore naturally to be given to the lessons to be drawn from the English system. In 1844 it was obvious that an undue number of institutions had issued notes, that in many cases the note issue had been unduly inflated, that financial stringencies and panics were very frequent, and that certain individuals in the banking business were discreditable. What was lost to sight was the outstanding fact that

the English system was not and had never been a free one. The Bank of England's monopoly had choked freedom. No bank had succeeded in overcoming its legal disadvantage to a sufficient extent as to be in a position to compete on equal terms with the favoured institution. To that cause could be directly traced all the alleged defects. The number of institutions was great because they themselves were unduly small, the issues were disproportionate to the cash resources because the cash resources could not be increased by adding to the number of partners, the inflation was due to the fact that the credit of the community was placed upon too few and too weak shoulders. The panics were traceable to the fact that these small institutions were not allowed to protect the meagre cash resources that they had.

If the arguments against freedom of banking were valid, logic would demand that the case would be best proved by examining the evil result of the system at the place where the freedom was greatest. Unfortunately for the economists, their case breaks down completely and utterly under such test. England afforded no criterion of the evils of banking freedom from the simple but overwhelming fact that English banking was never free. Where, then, shall we turn to apply the test? Surely to Scotland, the country that enjoyed the closest

approximation to free banking that the world has ever known.*

The first bank in Scotland was the Bank of Scotland, incorporated under Act of Parliament in 1695, one year after the Bank of England. It was a privileged institution like its English sister. Its charter was for twenty-one years. Its monopoly lay in the fact that it was the sole institution in the country allowed to issue notes.

Fortunately for the progress of Scotland, the bank fell out of the royal favour. In 1727 George I. granted a charter to another bank, known as the Royal Bank of Scotland, or more popularly the New Bank. There were now in Scotland two institutions of equal financial strength competing in credit. The result was marked from the outset. The dividend of the Old Bank fell from 22½ per cent. in 1727 to 3¾ per cent. in 1729, and up to 1743 the dividend averaged only 5 per cent.

The two banks competed fiercely. The Old Bank tried to wreck the other by cornering its notes, and by presenting them in mass for payment in gold. Unfortunately, its new weapon recoiled upon itself. The Old Bank's issue was much the larger, and therefore its notes were more easily obtainable in the open

* Conant, p. 142: "The Scotch system of banks of issue comes nearer to the ideal of successful free banking than that of any other country."

market. The New Bank adopted its opponent's tactics, gathered together the Old Bank's notes, and presented them. The Old Bank was thereby subject to sudden raids on its gold resources. In 1730 it was reduced to issue the option-clause note, a £5 note, payable on demand, or at £5 2s. 6d. in six months after being presented, at the bank's option. In 1732 it issued £1 notes with a similar clause.

In 1746 the British Linen Company was formed. At first a commercial firm, in 1750 it issued its own notes, and in 1763 it ceased its mercantile operations and became purely a banking house.*

In 1749 a small private firm in Aberdeen (Messrs. Livingston, Mowat, Bremner and Dingwall) was founded. It called itself the Banking Company of Aberdeen, and was the first private house to issue notes in Scotland.† This effort aroused the jealousy of the Old and the New Banks. They sent an agent to Aberdeen, who collected the notes of the new company and presented them for payment. The result was

* The three institutions had equal financial resources: Bank of Scotland, £100,000; Royal Bank of Scotland, £111,347; British Linen Company, £100,000.

† John Coutts and Company was the earliest private bank in Scotland. It was founded in Edinburgh about 1730, but apparently did not succeed in issuing notes, as Edinburgh was sufficiently catered for in this respect by the Old and New Banks.

that the private bank abandoned issue and was dissolved.*

In 1749 the Old Bank and in 1750 the New Bank attempted to start branch banks in Glasgow. The result is important as an indication of the *centrifugal* nature of free banking. The branches both became so independent that they broke away from the parent institutions. In 1757 the Edinburgh banks attempted to repeat their Aberdeen tactics against their own offspring. Their agents collected and presented notes for payment in the approved manner. But the Glasgow banks did not break under the strain. The Old Bank's offspring became the Ship Bank, the New Bank's offspring the Glasgow Arms Bank. The former was ultimately merged in the Glasgow Union Bank in 1838, while the latter carried on till the Napoleonic wars, when it paid its liabilities in full and suspended business.

The Royal Bank was very disposed to scoff at its older rival for protecting its cash resources by the use of the option clause, yet the practice in no way affected the people's confidence in the notes, which circulated at par. In 1761 a drain upon

* Kerr, p. 74: "A disinterested judgment must, in the absence of further evidence, ascribe the failure of this, the earliest attempt to establish that magnificent system of country banking which has proved one of the most distinguishing features of Scottish banking, to the prejudice and short-sighted self-interest of the two oldest banks."

the country's cash resources set in, the pressure emanating from England. Naturally enough the drain was felt by the Royal more than by the Old Bank, as it had no protection, and it was soon forced to adopt option-clause notes, its example being followed by the British Linen Bank the same year. Small private banking houses, as distinct from the chartered banks, were already springing up in the country districts, and these all adopted the option clause as an essential part of banking machinery.*

The other banks also found it necessary to follow the example of the Old Bank in another respect, that of lowering the denomination of the notes. In 1758 the Royal Bank issued its guinea notes, and other banks followed the same trend. Here we see the beneficial efforts of competition. Economic processes had decided that the pound sterling was the most convenient unit for exchange purposes. The Old Bank's currency was more convenient than that of its rivals, and therefore increased in volume. The others were forced to accept the situation, and

* The British Linen Company was forced to do so in self-defence. Its announcement states: "The very great scarcity of silver and the unwarrantable methods taken to carry it off, having induced the directors of the Royal Bank to issue notes with the like option clause contained in those of the Bank of Scotland and all the private banking companies, this measure of the banks has occasioned an unusual demand for specie for the Company's notes, and made it not only advisable but necessary to take the same precautions. . . ."

followed the public demand. The privileged Bank of England, with no rival of equal financial status, could afford to ignore and did ignore the competition of the six-partner banks, and did not issue £1 notes until the Napoleonic wars drained England's cash resources for export as foreign subsidies.

It must be borne in mind that the development of the option clause and the small note proceeded, not from firms of doubtful standing, but from the oldest and most substantial bank in a country of comparatively free finance. It was no artificial or unstable phenomenon, but a natural one.

Another consideration should be given due weight in estimating the progress of the Scotch banking system. Scotland did not possess the same cash resources as England. It had never had such a wealthy class of goldsmiths. Its most powerful banks were founded upon small resources.* When the Bank of Scotland started in 1695, the country was still to some extent a mere collection of clans, and the populated areas were separated by wide stretches of uninhabited waste or mountain ranges. The roads were poor, traffic was infrequent. The whole country had not developed economically as far or as evenly as England. Market towns were less common, merchant princes were rare. The cash resources of the

* The Bank of England was financed at £1,200,000, the three Scotch banks, combined, at £311,347.

country were so meagre that commerce could hardly be sustained. It was upon this unpromising soil that the world essayed the experiment of free banking.

The scarcity of cash resources exposed the system to a pressing danger. Any external call upon gold jeopardised the banks. These therefore quite early tried to strengthen their position by inviting deposits. In 1707 the Old Bank became a bank of deposit; in 1729 it allowed 5 per cent. interest on such deposits; and in 1731 it introduced the system of fixed-period deposits, paying 4 per cent. for twelve-month deposits and 3 per cent. for six-month deposits.

The example of Aberdeen and Glasgow was soon followed throughout the country. Private banks sprang up in many places. Undoubtedly some of these were mere mushroom institutions, lacking experience, resources, and integrity. They made exaggerated use of the good points of their older rivals. They issued quantities of small notes, and when these notes came back for redemption in gold they sheltered themselves behind the option clause.

The law-makers in 1765 met the situation by prohibiting both the note under £1 sterling and the option clause, the first piece of restrictive legislature in banking Scotland had known. The country had survived eighty years of banking with no great calamity, but with general increase of stability. Seven years after the suspension of the option clause

the first real failure occurred. The Ayr Bank (Douglas Heron and Company) had been formed in 1769. In 1772 it was financed at £130,000 by 241 partners. Its methods of business had been very risky, and several times it had been on the point of failure. Finally the Edinburgh banks refused to accept its paper, and it suspended payment. The ultimate loss to its partners was £663,000. It is doubtful whether the option clause would have saved it, though the absence of that clause precipitated the blow. Its methods were too unsound for ultimate success.

During the Napoleonic wars Scotland suffered the same drain as England. The option clause being removed, it had no protection. London called time after time upon its cash resources. Yet Scotland stood the drain much better than the industrial parts of England. When the English Government suspended cash payments by the Bank of England, the Scotch banks followed the example (1797). The shortage of cash became most pronounced.* Industry was threatened with ruin.

* Kerr, p. 145: "One of the most distressing features of the situation was the want of small currency. . . . Tradesmen could not pay wages and small purchases could not be made. People resorted to the expedient of tearing £1 notes in halves and quarters, a practice which appears to have been tacitly recognised by the banks. Eventually an Act was passed to permit banks to issue notes of less than twenty shillings' value for a limited period."

But the faith of the Scotch people in their tried and trusted banks was not shaken. No series of failures, such as occurred in England, was to be recorded. Instead, the soundness of Scotch finance was rendered more conspicuous by the trial. The restriction of 1765 was rescinded as regards the small note, and five-shilling notes were issued. The suspension of cash payments was, strictly speaking, illegal, as the order did not apply to Scotland, but no one tested the banks' action at law. During the time of suspension Scotch notes retained their par value, whereas the notes of the Bank of England fell to a discount.*

Upon the resumption of cash payments in 1826, the English law-makers tried to abolish notes under £5 in Scotland as well as in England. The attempt was a failure. The nation had experienced the value of the small note issued by reliable banks, and was prepared to secede from the union rather than be robbed of them. Not only Scotland but England also was slowly learning their value. The northern counties of England—Cumberland, Westmoreland, and Northumberland—preferred them to English notes, and petitioned Parliament to allow their circulation to continue.†

* Kerr, p. 146.

† Graham (p. 298) quotes the memorial which reads: "An Act of Parliament limited the number of partners in our English banks to six . . . while the absence of any such limits in Scotland gave a degree of strength to the issuers of notes which several banks

The great crises of the early part of the nineteenth century, ruinous as they were to English traders, hardly affected Scotland with its better banking system. Yet so imbued were the advocates of credit restriction with the certainty that they had complete understanding of financial principles, that they inflicted the principles of the 1844 Act upon Scotland in 1845. The latter Act prevented new banks of issue in Scotland, abolished notes under £1, and limited the issue of notes not represented by gold. Thenceforth Scotch banking possessed no essential advantage over English banking.

During the century and a half that Scotland enjoyed free banking it rose from an obscure and backward country to one of the most industrial communities the world had ever known.* In spite of the comparative barrenness of the soil, its agriculture ranked among the best in the world. Farm leases were lengthened to nineteen years, whereas in England they rarely extended to more than one

established in our counties have not been able to command . . . in the course of the last fifty years, with the solitary exception of the Falkirk bank, we have never sustained the slightest loss from one acceptance of Scotch paper; while, in the same period, the failures of banks in the north of England have been unfortunately numerous, and have occasioned the most ruinous losses."

* Kerr, p. 11: "The history of banking in Scotland is most intimately associated with the national progress from poverty to wealth."

year.* Its engineers became world famous. Its prosperity was manifest, and was untroubled by those recurring financial spasms that caused such havoc in England.

The historical test, then, affords complete proof of the superiority of free banking over restricted banking. All attempts to refute the proof have been remarkably lame and far-fetched. Jevons affords an amazing instance of reasoning. Scotch banking was successful because only a few sound firms issued notes. English banking was unsuccessful because many unsound firms issued notes. The explanation cannot possibly be that freedom in banking is good, because economic doctrine has already postulated that it is bad. The reason must lie in the fact that Scotchmen are Scotchmen !†

* *Encyclopædia Britannica*—Article "Scotland": "It was not until after the abolition of hereditable jurisdictions in 1748 that agriculture made real progress. . . .

"The system of nineteen years' leases had proved distinctly superior to the system of yearly tenure so general in England."

Beer, M., *A History of British Socialism*, 1921, vol. i., p. 97: "From 1775 onwards the pioneers of land reform have been Scotsmen."

† Jevons, p. 319: "Up to 1845 the twelve or thirteen Scotch banks certainly did possess the right of freely issuing notes down to £1 notes, and only in one or two cases did bankruptcy occur. . . . If we were all Scotchmen, I believe the unlimited issue of £1 notes would be an excellent measure. But when we compare the Scotch and English banking systems, we discover a profound difference. In Scotland there exist only eleven great banks which take good

The outstanding difference in stability between Scotch and English banks is shown in the fact that the English banks existing to-day were founded after the six-partnership restriction was removed (1826) and have no right of note issue. On the other hand, the present Scotch banks were all founded at intervals between 1695 and 1838, and have retained their right of note issue. The inference to be drawn from this is that, apart from legislative restriction, the note-issuing bank is the most stable form.

Let us apply the test to another country.

Banking development in Ireland has most of the aspects of Scotch banking, with the one important exception that the Bank of Ireland had a privileged position, closely akin to that of the Bank of England. The earliest bankers were goldsmiths and general traders, who, however, were limited in their operations by severe usury laws. Their business was sufficiently extensive for their bills to be recognised

care that there shall not be a twelfth great bank. In England and Wales we have 267 private and 121 joint stock banks." Time has proved Jevons wrong in every detail. Four of the big Scotch banks were established in 1836–38. It was the application of Peel's Act to Scotland in 1845, prohibiting fresh banks of issue, which stopped further banks being formed. On the other hand, the Big Five, by their control of the cheque clearing house, prevent any further big banks being formed in England, and have succeeded in absorbing almost all those existing in Jevons' time.

by law in 1709. The condition of the country was much worse than that of Scotland when banking was introduced.* Cash resources were very small, and, as Ireland was dependent upon England for coal, such meagre cash stores as the country possessed were constantly being drained away. Many failures attended early attempts to found banks. The law discouraged substantial men from entering the business.† The Government was weak and administration was corrupt. In 1767 some seven or eight banks had succeeded in establishing themselves, but after 1770 no new banks were founded. Several projects were brought forward from 1724 onwards to establish a chartered bank similar to the Bank of England and the chartered banks in Scotland, but popular feeling was at first very unfavourable. It was alleged that such a bank would discourage banking enterprise, would be a Protestant concern, would be a tool of England, and so on.

In 1782 the Government was in debt and the Treasury empty. To procure money the Bank of Ireland was chartered. It was to be financed at £(Irish)600,000 (=£553,800 sterling), of which

* See Dillon, p. 27: "Whiteboys, cattle houghers, and midnight robbers ravaged the country, murdering people, killing and torturing cattle and burning houses, in defiance of half-hearted attempts to secure peace and order."

† Dillon, p. 27: "The legal restriction imposed on bankers . . . prevented capitalists from embarking in the business."

not more than £10,000 could be held by one person, and its resources were to be lent to the Government at 4 per cent. The Bank obtained the same privilege as the Bank of England, that no other bank throughout the country having more than six partners should be allowed to issue notes, a monopoly which remained in force till 1820, when its scope was limited to a radius of sixty-five miles from Dublin.*

Ireland suffered, with England and Scotland, the cash drain of the Napoleonic wars, and the Bank Restriction Act of 1797 was applied to it. This immediately encouraged the creation of numerous flimsy six-partner banks which shared the fate of their English brethren.† Between 1797 and 1800 many banks were founded and failed, leaving only eleven still existing in 1800. In 1804 the number rose to over fifty, but dwindled to thirty-three again in 1812. At the time of Waterloo (1815) the number had fallen to thirty-one, and with the return of peace many of these disappeared, so that in 1820 there were only six remaining.

* See Dillon, p. 45: "In the light of later events, the toleration of so burdensome a monopoly for a period of forty years is almost inexplicable, and its subsequent removal marks a period in the commercial prosperity of the country from which all after progress can be plainly traced."

† Dillon, p. 29: "The Bank Restriction Act . . . led to largely increased issues on the part of the Bank, and was accompanied by a corresponding increase in the issues of private banks."

The limitation in 1820 of the Bank of Ireland's monopoly to within sixty-five miles of Dublin opened the way for other stable banks. The Northern Banking Company and the Provincial Bank were founded in 1825. The Belfast Banking Company, the National Bank, the Ulster Bank, and the Royal Bank of Ireland were founded between 1827 and 1836. The Hibernian Bank was founded in Dublin in 1825, and tried to challenge the Bank of Ireland's monopoly by issuing paper tokens not expressly promising to pay gold. These tokens bore the words, "Hibernian Bank Token. One Pound." This attempt at evasion was defeated at law by the Bank of Ireland.

Ireland followed Scotland in the use of £1 notes, with the result that such notes were soon more acceptable than gold, for the reason that the banks took greater care against forgery than the State did against counterfeiting.*

Bad as were political conditions in Ireland, the country throve under private banking. In 1800 the population was over 5,000,000. It increased until in 1845 it was over 8,250,000. The application of Peel's Act to Ireland in that year marks the apex of

* Mr. J. McNamara, in his evidence before the House of Lords in 1826, stated: "The country people were afraid of gold, because they were not assured whether it was gold or not . . . but if they are furnished with a note, the person giving it puts his name upon it, and that gives them an assurance."

its prosperity. The limitation of note issue at once caused a restriction of credit. The banks were forced to protect themselves by withdrawing gold from circulation. Deposits increased from £M8 in 1845 to £M8½ in 1846. Agriculture was an immediate sufferer. In 1846 and 1847 Ireland experienced the worst potato famine in its history, during which thousands perished. From that day a steady decline set in. In 1851 the population had fallen to 6,500,000, in 1861 to 5,800,000, in 1871 to 5,412,000, in 1881 to 5,175,000, and in 1911 to 4,382,000.

In still one other country can a comparison be made between the merits of free and restricted banking. In U.S.A., until the Civil War of 1861–64, the individual States were the effective political entities. Since that war political power has been centralised in the Federal Government. After the Declaration of Independence (1776) two attempts at conducting a National Bank had been made, but the second National Bank was suspended in 1837. From 1837 to 1861, banks controlled by State legislature, as distinct from Federal laws, were the only banking institutions in the country. In a territory so vast and under legal systems so varied many different types of institutions were founded. They can be grouped into four main categories: (1) Free note-issuing banks; (2) those issuing notes

secured by general safety fund imposed by law; (3) those issuing notes based upon public securities; (4) State banks controlled by the legislature.

Experience showed conclusively that the first type of bank was the most useful and reliable.*

The best system of banks was in Massachusetts, where the greatest freedom prevailed. The failures were rarer there than elsewhere, and financial stringency which caused panics in other States scarcely ruffled the surface of Boston business. On the other hand, the attempts of the States to conduct banks for themselves form the record of the most melancholy failures in economic history.†

Kentucky, Alabama, Mississippi, Florida, Arkansas, Illinois, Tennessee, Louisiana, Indiana, Georgia, Vermont, Missouri, Delaware, the Carolinas, all succumbed to the fatal snare. The credit of a bank, supported by the faith and credit and wealth of the State, appeared to be sounder than that of a private bank. There is to-day inscribed in the constitution of those States a testimony to the fact that the State bank is the unsoundest of all forms of

* Conant, p. 393: "The experience of the New England and Indiana Banks is the triumphant vindication of the principle of banking on general assets and issuing notes redeemable in coin on demand."

† Conant, p. 378: "One of the most dismal chapters in American banking history is that which records the creation and collapse of banks owned and managed by the States."

banking. Even in Indiana, where the State bank was not the utter failure that it proved to be elsewhere, the condemnatory clause stands in the Constitution.* The Kentucky State bank (Bank of the Commonwealth) ceased to loan money under an Act which was passed when it became evident that no one cared to borrow the kind of money that it issued.

In Illinois the notes and stock of the State bank were burnt on two occasions in the public squares of Vandalia and Springfield, in the presence of State officials, as a public testimony to their worthlessness.

In Alabama the climax was much worse. It has been computed by one of the Governors of the State that $1,000 per diem is still being paid by the people as the price of their forefathers' folly. The direction of the bank sank into the hands of politicians, five out of the thirteen of whom were hotel-keepers. No director could refuse a discount to a member of the legislature. All taxation was abolished and Government expenditure was met by the paper of the State bank. Ultimately the flood of such paper alarmed the community, and the

* Indiana Constitution, 1851: "The State shall not be a stockholder in any bank after the expiration of the present bank charter." Alabama Constitution, 1867: "The State shall not be a stockholder in any bank, nor shall the credit of the State ever be given or loaned to any banking company or association or corporation." Similar clauses exist in other State constitutions.

edifice collapsed, precipitating with it the commercial prosperity of the community.*

The experience of Mississippi was even more tragic. Henry V. Poor describes the situation upon the failure of the State bank as follows: "The $M48 of loans were never paid, the $M23 of notes and deposits never redeemed. The whole system fell, a huge and shapeless wreck, leaving the people of the State very much as they came into the world. Their condition at the time beggars description. Society was broken up from its very foundations. Everybody was in debt, without any possible means of payment. . . . The only personal property left was slaves, to save which, such numbers of people fled with them from the State that the common return upon legal processes against debtors was in the very abbreviated form of G.T.T.—*gone to Texas.*"

Every test that can be made of the comparative merits of free and restricted banking points to one conclusion and to one conclusion only. Where the banks were freest, the system was soundest. Where the banks were controlled, the system was defective, and the greater the control the more worthless the banks.

* Conant, p. 382: "Confidence in the paper money, 'supported by the faith and credit and wealth of the State,' to use a favourite phrase of the champions of Government paper money, suddenly collapsed, and with it the whole structure of business and credit in Alabama."

It is extraordinary that, in face of such evidence, the economists adhere to the heresy that State control of banks is a necessary factor of economic life. It is almost incredible that in a country such as England, where Free Trade has been accepted as essential to progress, no serious effort has been made to apply Free Trade principles to finance as well as to commodities. The explanation can only be sought in the fact that the minds of economists and statesmen have been enslaved by an obsession, which has controlled them so absolutely as to blind them to an obvious truth.

The argument of the economists in favour of banking control is remarkable for its very perversity. The point they wish to establish is that freedom of banking means overissue of notes and financial instability. To support such a contention reference is made, not to economic fact, but to a hypothetical case. Pierson's statement of the case, quoted approvingly by other economists, is as follows: "Suppose a bank's note circulation amounts to £M18, against which it holds a metallic reserve of £M8. It grants loans for a further £M2, but the public does not require more than £M18 in notes; the extra £M2 put into circulation will therefore cause a redundancy of money. It now becomes advantageous to export coin or bullion, and that coin or bullion is obtainable at the bank in exchange

for notes. The extra £M2 will now return to the bank, and the circulation will be again reduced to £M18. But against these £M18, the bank's reserves will now be only £M6. The bank may pursue this course for a long time. It may increase its loans up to £M18, the amount of its note circulation remaining all the while at the old figure. But the whole reserve—that is, the guarantee of the convertibility of the notes—will have been exhausted."*

This is a similar kind of mental trick to that practised by Bastiat in his explanation of interest.† It is not economics, but imagination. True it is that under a free system an isolated case similar to the above might possibly happen, just as under free contract William and James might agree that a plank was a fair interest for the loan of a plane. But to use an imaginary isolated case as a representation of an economic trend is simply to toy with reasoning.

Let us examine the case. A bank has a stock-in-trade of £M8 in metal. It overissues notes. Its metal stock falls to £M6. It continues the process; its metal stock falls to zero. The bank then has wilfully squandered the whole of its stock-in-trade. What has it got in return? Nothing. If a bank were to do such a thing it would injure

* Pierson, N. G., *Principles of Economics*, vol. i., pp. 459–460.

† See pp. 173–4.

itself more than the community. Banks conducted upon such lines would succumb, and stable banks would replace them.

It is also unnecessary for Pierson to assume that the gold would go abroad. The greatest critics of banks in a free system are the other banks of that system. If any bank should overissue, the other banks would suspect it, and would return the guilty bank's notes for redemption. The result would be that the cash resources of the unsound bank would find their way largely into the possession of the sound banks.

The centripetal school of finance cannot indeed make up its mind upon this point. The danger of overissue is a nightmare to be conjured up whenever freedom of finance is advocated. Should the question be that of strengthening the centripetal system at the expense of the community the opposite argument is used. Thus, Mr. J. H. Schiff, a well-known international banker, proposed in 1906 the founding of a central bank of issue. His proposal, which was accepted by the New York Chamber of Commerce, was supported by the antithesis of Dr. Pierson's argument: "A central note-issuing bank would supply," he urged, "an elastic currency varying automatically with the needs of the country. This currency could never be in excess, for notes not needed by the country would be presented for deposit or redemption."

Mr. Schiff's argument is not sound when applied to a *central* bank of issue, because such a bank would speedily obtain powers to make its notes a forced currency, in which case they would depreciate in value, prices would rise, and the volume of notes in circulation, instead of decreasing, would constantly increase. This is the actual phenomenon which is occurring all over Europe to-day, and is threatening to wreck civilisation. The argument is, however, extremely sound when applied to a free bank of issue where competition from other banks of issue is allowed.

Further examination will show that the argument of the economists recoils upon themselves. It is not a criticism of free banking, but a condemnation of the present system.

Gide is of opinion that freedom of issue will be dangerous, and must be obviated by control. Strangely enough, the system of control, he admits, produces exactly the dangers from which he is trying to find a means of escape.*

He is of opinion that control is essential in the public interest. Overissue by imprudent note-issuing banks would inflict loss upon the community,

* Gide, p. 434: "We cannot disguise the fact that absolute freedom of issue may give rise to grave dangers, at periods of crisis anyhow, if not during normal times. Now, crises are becoming more and more frequent in the economic life of our modern societies."

and must be avoided at all costs. How he is in a position to know that freedom would involve overissue is not clear, as he states that no free bank has ever existed.* Equally with Pierson he is guilty of mistaking the supposition of a fertile imagination for the verdict of economic history.

Imprudent banks do exist, but they are not the free banks of the economists' imagination. They are to be found in actual reality within the present industrial organism. They are the State banks or semi-State banks, which lend on paper evidences of debt rather than on ability or real wealth; which subordinate their soundness to political considerations; which have become the tools of war instead of the instruments of peace; which have saturated the community with an excess of forced currency under the legal tender laws.

This is a severe indictment, but it deserves

* Gide, p. 434: "True, the notes issued in too great a quantity by such an imprudent bank would come back for repayment as soon as they depreciated; but depreciation does not make itself felt instantaneously. It may not be felt for some weeks; and if, during the interval, the bank has continued to throw into circulation an excessive quantity of notes, when these come back it will no longer be able to pay them, and will sink, as it were, under the ebb-tide of circulation. Of course, by its failure the bank will be the first to be punished for its imprudence. But what good will that be to us? Our concern is to prevent the crisis, not to punish the authors of it. The system of absolute liberty, indeed, without any regulation of issue, has never been practised in any country."

serious attention, as the accuser is none other than an economist who defends State control of banking.* Gide cannot hide from himself the fact that the State banks are influenced by unsound considerations, and that their note issue was, even in pre-war days, excessive. What, then, is to be said of their position to-day? If francs M6,800 was too large an issue for the Bank of France, is not the francs M25,000 of notes, the uncovered issue of to-day, a public danger? Are not the French people realising their danger when the value of the franc is greatly depreciated, when they can only with difficulty purchase from abroad raw materials for their vital industries? Are they not, in fact, paying rather too dearly for insurance against the imaginary danger of an imprudent overissue by a hypothetical free bank?

* Gide, p. 437: "The third method consists in fixing a maximum of issue. This is the system practised in France, the maximum being francs 6,800,000,000. But what safeguard is there in limiting the issue if the Bank is able to reduce its metallic reserve to zero? Where is the guarantee for the public? Solely in the prudence of the Bank, which will endeavour to maintain a wise proportion between the metallic reserve and the circulation. A figure of nearly francs 6,000,000,000 of notes in circulation which may be raised to francs 6,800,000,000 is, however, excessive and dangerous, and is justified only by political considerations. The idea is that the Bank should have the strongest cash reserve possible in order to serve as a war chest, and it is evident that if the Bank is not to draw on this for its discount and transactions it must continue to issue notes."

The economists have sought to bolster up an artificial and state-controlled system of banking by depicting the dangers of decontrol. Economic history refutes their arguments. Their own evidence shows that the dangers they fear are inherent, not in free banking, but in the very system which has been fostered to obviate those dangers.

Carlyle dubbed orthodox economy the "dismal" science. A more fitting name would be the "topsy-turvy" science. It has built imagined facts upon preconceived theory instead of building its theories upon the bed-rock of fact. Nemesis has been and is inevitable. All the conceptions of the economists have one by one been shattered. Their greatest delusion, centripetal finance, stands condemned from the overwhelming mass of evidence afforded by the dismal spectacle of a whole continent of industry verging on bankruptcy before our very eyes.

The difference between the present artificial and the natural system of finance lies in one characteristic. The present system is tied to gold. The natural system shows a tendency to escape from gold as far as possible, and to create an instrument of exchange based upon real wealth or constructive ability.

The function of an instrument of exchange is to exchange wealth, either already produced or about to be produced. Economic progress is a change from

production for self to production for others—that is, production for exchange. This can only be achieved by the use of a suitable instrument. In the rudimentary economic system of the Middle Ages, certain commodities were accepted as filling the rôle. Ultimately gold triumphed over its predecessors because it was the most exchangeable commodity. From being merely a commodity like all other commodities, gold became a recognised claim upon all other commodities. As its claim was recognised by all, it became the medium of exchange. Division of labour and increase of production threw a greater and greater strain upon gold, until society was forced by natural law to evolve a better system of currency.

The medium which was slowly being evolved to replace gold was a paper claim upon wealth, issued by creditable persons, possessing circulating power equal to or greater than gold and sharing all its attributes, except its material substance. The community had to educate itself to the soundness of the new medium, and safeguarded itself by the natural test, that, in case of doubt as to the value of the note, the latter might be converted back into gold. As the value of the note became more generally recognised, the gold backing was less necessary. In other words, the issuing bank could circulate more notes upon a given gold reserve.

These notes, however, being a claim upon commodities or real wealth, could only be issued to producers of real wealth, the promoters of industry. Gold was by the very nature of the process fated to drop more and more into the background. Complete detachment of the note from gold was and must always remain impossible, since the note should be a claim upon all forms of wealth, and must be able to purchase gold equally with any other commodity.

The banks of issue, therefore, very wisely issued notes in denominations which practical experience had shown to be of most service to the community. The most convenient units of exchange were the pound and the ten-shilling piece. To this experience every bank, except the aristocratic State-controlled banks, conformed.

When financial development was forced into an unnatural channel by the theorists of the Currency Principle, the note had already achieved a part of its mission. It was accepted, where issued by a creditable institution, as a claim upon wealth. It had also retained, as a natural safeguard, its claim upon gold. Anyone who was unwilling to accept the note could revert to the old system by converting the note into gold.

The note was in its origin merely a claim upon gold, but had become more and more recognised as a claim upon all forms of real wealth. To be more

concrete, anyone could take a note issued by a creditable bank into any shop and be reasonably certain of being able to buy goods. On the other hand, anyone could take the note back to the bank and be reasonably certain of getting gold for it. Centripetal finance has changed that completely. It has substituted for gold, in place of the circulating note of even and convenient denomination and reasonable security, a non-circulating cheque of varying denomination and uncertain security. The result can be tested anywhere. The cheque is not a generally recognised claim upon real wealth. It cannot be used in the daily life of the masses for wages or for the purchase of goods. Its characteristic is not to circulate but to be sent back to the bank for clearance. The need for a circulating medium is constantly increasing, but no substitute for gold is allowed. Since interest is the toll extracted for the use of the call upon the circulating power of gold, interest rates tend to rise. Hence the gold stores attract a greater and greater yearly accretion, and the centripetal tendency of finance is increased.

If the natural right to issue notes were restored, the process would be slowly but surely reversed. The notes would make their way gradually into circulation. Their value at the outset would be frequently tested by conversion into gold. As the community proved the stability of the competing

banks the unsound ones would withdraw from the field or alter their methods. The increased confidence engendered by the greater credit of the banks would lead to still further issue of notes. The banks would learn that issues must be made only to those persons who could produce real wealth. The notes issued to a non-producer would not represent real wealth and would become redundant. They would therefore be returned to the bank of issue. At present banks give credit to persons possessing mere saleable titles. These titles are more frequently evidences of debt than evidences of wealth. Under free note issue the tendency would be in the reverse direction. There would be no cataclysmic change, no violent upheaval of system. Nevertheless, it would be to the interest of the banks to issue their notes to as great an extent as possible in those directions where circulation was assured—that is, to the producing members of the community. The presence in the financial world of a competing instrument of circulating power equal to, or greater than, gold would force down the rate of interest. This would stimulate production, just as the increase of the rate discourages it. Men of productive ability, who are under the present system debarred from initiating new industries by the want of credit facilities, would find their path easier. Their success would increase the demand for labour. That would

ensure the payment of a better wage to the labourer. As competition among employers for workers increased, the worker's wages would approximate more and more closely to, and finally equal, the full value of his product.

In such a system the note would be a real credit instrument. It has no relation to the currency note of to-day which circulates under State fiat. The State currency note is not a credit instrument, but a coercive instrument. It is not for practicable purposes redeemable in gold, and has therefore fallen to a discount.* A golden sovereign is still worth 4·86 dollars, but the currency note is worth less than 4 dollars.

Equally with the State note, evidences of public debt are not pure credit instruments. They have their value ultimately in taxation. There is no natural corrective to the issue of coercive instruments, such as exists in the case of credit instruments. A free bank cannot overissue without loss of credit. Every State in Europe has in recent years overissued its paper money. Under free banking no firm could for long obtain an overcredit, since it must ultimately produce goods to cover that credit, or be unable to repay the bank. Every State has, however,

* This depreciation of State paper currency disproves Jevons assurance (p. 66). "No doubt in times past kings have been the most notorious false coiners and depreciators of the currency, but there is no danger of the like being done in modern times."

overissued evidences of debt to such an extent that it is doubtful whether the extreme measure of endurable taxation will enable it to pay its interest charges. The limit of disaster in a free financial system is individual bankruptcy, and the penalty falls with its maximum incidence upon the greatest offender. The limit of disaster in State-controlled finance is national bankruptcy. Its main incidence falls not upon the chief offenders. In the first instance, it falls upon the wage earner and small producer, then it strikes the larger producer, and ultimately it drags down the whole nation to disaster. To that end the nations of Europe appear to be drifting.

Chapter Ten: *Disruption or Progress*

WHATEVER highly industrial society we may examine at the present time, the dominating characteristics are those of dislocation, upheaval, and disruption. It would appear reasonable to expect that, after the enormous scientific developments of the last two centuries, the various countries would have evolved a system of steady and constant progress. The reverse is the case. The potential production of wealth is impeded and harassed by strikes, disputes, agitations. The strikes have progressively increased in frequency, in extent, and in intensity. The disputes have become more acrimonious and the agitations more violent. The economic machine is shaken, jolted, and battered. It still has sufficient efficiency to function in spite of the tremendous buffets it has received, but it is showing symptoms of complete breakdown.

In England the situation is only tolerable in comparison with the more unhappy lot of its Continental neighbours. Trustification has made headway since the Armistice at a more rapid rate than before the war. The large firms have expanded to an unprecedented extent, have absorbed or displaced their smaller rivals in an astonishing manner. Credit restrictions have jeopardised the industrial

community. Strikes have inflicted unnecessary hardships upon the workers themselves. Unemployment is a gaunt spectre before which statesmanship recognises its impotence.

All the ideals cherished since the Reform Bill of 1832 are endangered. Political democracy is threatened by industrial revolution. Parliament is an illusion, and the real fight is being waged outside its chambers. A small group of semi-irresponsible ministers is endeavouring to feel its way through the industrial storm-centre. It condescends, from a traditional sense of duty, to consult Parliament after action has been taken. The model legislative assembly of the world is now a mere registry, which records the acts of ministers without having any directive voice. The Labour movement is fitfully controlled by dominating personalities formed into conflicting groups. The control passes from one side to another, but the general tendency is toward the extremist wing.

The workers are pawns in the game, the stake of which is the control of the nation's destiny. Here and there they snatch, after disproportionate effort, a slight increase in the face value of their wage. More often they have to consent to progressive reductions. The loss of purchasing power attaching to their wage is constant, and leaves them baffled, angry, and suspicious.

The tradesmen are alarmed and uneasy. The post-war boom has disappeared. The effective demand for commodities has vanished. Stocks are unsaleable, and credit is unobtainable. Bankruptcy haunts them as the final outcome of years of endeavour and hope.

The banking world appears equally disturbed. The clamour for credit cannot be met. The vast mass of titles to public debt cannot be absorbed. The trade of the country cannot be sufficiently financed, and the end is not in sight.

The statesmen make frantic efforts to settle the more acute troubles as they arise, but each one is disposed of only to clear the stage for still more critical ones. Every prophecy has been belied, every hope frustrated. The peace after the war brought not security but disturbance, not goodwill but rancour, not calm but storm.

The American position does not appear conspicuously better. That country is in the throes of economic violence. Strikes and wage feuds are prevalent. Credit is difficult. Financial interests are unsettled. Money rates fluctuate violently.

The Continent of Europe presents a wellnigh hopeless spectacle. France is overloaded with debt, and snatches at the vain hope of saving itself by bleeding still further an almost bloodless Germany. Germany sinks lower and lower into the abyss,

and is only deterred from violent upheaval by the spectacle of the Russian economic debacle. Italy has lost hope of succour from its former allies. Disruptive forces are strong, and the government is powerless. Outbreaks occur sporadically in the industrial centres. Workmen seize the factories, only to find they cannot sell the products.

Even the neutral countries, in spite of the increased gains acquired during the war, cannot finance their requirements. They are obliged to seek help from America upon unprecedented terms.

Russia has been through its ordeal of fire and has emerged, to sink into economic dissolution. Its manufactures and its transport are threatened with extinction. Its credit system is decrepit. Its population is ill-clothed and starving.

So awful is the story of distress from Continental Europe, and so impossible is the task of rendering effective aid, that even the sympathetic have adopted the course of closing their ears to the tale of human misery. That Russia is threatened with economic barbarism, that Vienna is suffering from famine and disease, that the children of Germany are growing up rickety and undersized, all this may be true, but the gravity of the problem elsewhere leaves little inclination and still less power to aid.

Russia struggles to readjust its broken organism. Germany looks to France for mercy. Italy and

France seek the aid of England. England sees no way through her own difficulties, and would fain obtain help from America. America is occupied by dealing with its own real troubles, and manifests an obvious intention of allowing the rest of humanity to work out its own salvation or to go in its own way to its doom.

Internationalism is a vanished force. Each nation is a struggling unit, endeavouring to regain or retain its place without regard to the difficulties either of its enemies or of its quondam allies. International congresses meet and discuss and avow themselves powerless to act. Ancient alliances are threatened, and ancient enmities are masked by the common woe. The world is split up into national entities, envious of the more prosperous, apathetic towards the more miserable.

Everywhere the forces of disruption are in evidence: disruption not only of the world as a whole, but of nations and of races and classes within the nations, of sections within the classes; disruption of the financial system, of the industrial machine; disruption of moral principles and social order.

It may be supposed that the present condition of the industrialised world is the result of the war. That is not the case. The war undoubtedly intensified and brought to a head the many symptoms of

disruption, but a more thorough diagnosis will show that every symptom can be traced to pre-war days. In some cases the war has given such symptoms a national aspect instead of a sectional one; in others it has intensified an already existing national disruptive force.

The factors which are now working together to bring about complete disruption of the economic organism are, we repeat, not the result of the Great War. Militarism, intensive nationalism, tariff wars, aggressive financialism, class war, credit starvation, unemployment, underpaid employment—all these were present and increasingly evident in the pre-war period. Many secondary causes may be alleged as explaining them, but the one underlying and determining cause is the unnatural and artificially created system of centripetal finance.

The *human* mobilisation for the Great War was set in operation in the summer of 1914. It was to send some 50,000,000 men to the battle-fields of Europe, to meet death or to waste valuable years of their short span of life in the most aimless and destructive kind of existence. It was to divert the remainder of the population from the production of useful wealth, to turning out every form of death-dealing instrument that perverted ingenuity could imagine. It was to drag into the vortex of warfare the feminine portion of the race. It was

to load future generations with an inextinguishable debt. Yet the human mobilisation was but a secondary phase of the great preparation. The primary and determining step was taken much earlier.

The *political* mobilisation for the Great War can be dated from 1904. The defeat of the Russians by the Japanese at Mukden seemed to crush the hopes of revenge which had been nourished in France since 1871. Germany immediately took an aggressive line in diplomacy. The commerce of Morocco was made the object of a quarrel with France, and the famous French minister Delcassé was sacrificed to the needs of the situation. The same year, however, saw the origin of the *Entente Cordiale*, the first step towards a regrouping of Powers which was ultimately to surround the Central Empires with a ring of opponents. In 1908 Russia had not yet sufficiently recovered to make an effective protest against the annexation of Bosnia and Herzegovina by the Austrian Emperor. For the moment the Central Alliance held the upper hand. The German Emperor was prepared to support his Austrian confrère to the end. He announced that he stood "in shining armour" at the side of his ally. It was evident that war was a probability. The French and German Governments had already foreseen the trend of events, and were taking steps to meet the emergency.

The *financial* mobilisation of the war dates from 1906. In that year the future combatants put into operation their programme of fortifying the State-controlled banks. Germany supplemented the notes of 100 marks by notes of 50 and 20 marks, with the object of increasing the gold reserve for future war contingencies. In the same year the French Government authorised the Bank of France to increase its note issue to francs M6,800.* Military exigencies had caused Russia to issue small notes in 1904, and after the Austrian annexation of 1908 small notes of 10, 5 and 3 roubles were again forced into circulation. In Germany, early in 1914, the 50 and 20 mark notes formed no less than 26 per cent. of the circulation, and the Reichsbank's gold reserve had risen from £M39 in 1912 to £M67 in June, 1914. On the eve of the war the Bank of France had mobilised a gold store of £M165 and Russia of £M164. Half the gold-mining industry of the world was diverted to the object of providing the sinews of war for the coming struggle. Of the world's gold production during the eighteen months from January 1, 1913, to June 30, 1914, 30 per cent. went to the arts, 20 per cent. to India, and the remainder to the State banks of Germany, France, Russia, and Austria-Hungary.†

The *real* mobilisation for the war was carried out

* See Note 253. † See Conant, p. 743.

by the State-controlled banks. The war was financed by issues of paper money by those banks. Without such aid the war could not have taken place and without the privileges of legal tender it could not have endured six months. The State banks have loaded the world with a huge volume of depreciated paper money, and are now unable to call a halt to the vicious system they have put in motion. Those central banks of issue, whose claim to existence is alleged to be that they impart financial security to a naturally unsound economic system, have been the principal means of producing military and financial disruption throughout the universal social fabric.

The attempt to found an effective League of Nations is counterpoised by the recrudescence of intensive nationalism. While national interests are gaining increasing hold upon the minds of people, it appears somewhat idle to suppose that those interests will be reconciled by a pious allegiance to an unsubstantial concept. Is it likely that the rapidly widening rift between England and Ireland will be bridged by English and Irish representatives sitting in congress in Geneva when Irish representatives refuse to sit with the English brethren in Westminster? The recrudescence of nationalism in Ireland is no isolated fact. It has its counterpart in the growing animosity of the Flemish towards the

Walloon in Belgium, of the Hungarian towards the Austrian. Even in pre-war days symptoms of the same trend could be traced in the separation of Norway and Sweden in 1905, in the increasing girding of the South German against the Prussian, of the Catalonian against the Spaniard.

It might be supposed that economic development would tend to appease racial differences. As the communities become more and more interdependent traditional animosities should tend to die out. Scotland and England overcame their old enmities under the beneficent influence of trading interests. The Northern and Southern States of America forgot the Civil War as their economic interests blended. Unfortunately a strong counter-current must be charted. Economic development has not been even. Certain classes and races have benefited unduly, others have been woefully penalised. Well-intended attempts by legislation to redress the balance have called into existence huge burdens of taxation and large armies of civil servants. Tax collectors and bureaucrats are eyed askance even when they serve their own nationality, but when they are the servants of a different race the smouldering unease breaks out into open hostility. Irish antagonism to Dublin Castle is paralleled by the Flemish antagonism to Walloon State universities. Catalonian separatism is nurtured by the excessive

centralised power of the Madrid Government. The Prussian official is hated by the good-humoured South German. Centralisation in politics and centralisation in finance go hand in hand, but the latter is the dominating factor. Because centripetal finance has placed the wealth of the country in the hands of the few, social problems have assumed national importance. The State has been compelled to step in to protect the defenceless individual against the tyranny of the financial corporation which its own legislation has fostered. It has been obliged to tax wealth accumulations to succour the needy. In doing so it has created excessive taxation and an overloaded bureaucracy. One reflex of this inordinate State control is the re-growth of intense national feeling which is threatening to bring civil war in more than one composite nation.

Another factor which is doing much to nullify every effort towards an international understanding is the strengthening of tariff walls. The doctrine of Free Trade is to-day almost a spent force. The great movement of the first half of last century accomplished but a tithe of the results hoped from it. It gave England a short period of comparative superiority in trade. Up to 1872 the Free Trade country outdistanced its competitors. But from that time onward the competitors have been

gradually overhauling the leader.* Between 1860 and 1870 British exports increased by 47 per cent. Between 1870 and 1895 they increased by only 25 per cent. In contrast to this German exports between 1860 and 1870 increased by about 40 per cent., and between 1870 and 1895 by over 100 per cent. The reason is not to be sought in the comparative merits of Free Trade and Protection. Germany has a larger free trade area and a larger free trade population than Britain ever had. Inside the Zollverein there is complete free trade as understood by the Manchester school. The reason that Britain progressed more rapidly than other countries up to 1872, and more slowly afterwards, is that before that date it was trading upon a gold basis, while the others were still endeavouring to trade upon a silver basis. Germany adopted the gold standard in 1873, and immediately forged to the front.

* Tickner, p. 612: "The growth of our national industry and commerce reached its climax about 1873. After this, Continental competition began to be more keenly felt. The great extent of the market, now a world-wide one, and the increased opportunities for speculation, sometimes of a careless and reckless nature, caused this growth to be accompanied by periods of great depression following on periods of rapid trading expansion. The old stability of employment of the Middle Ages has long since disappeared. The periods of trade stagnation and depression which succeed the periods of overproduction have been accompanied by much unemployment and sometimes by commercial crises, with many serious failures in the business world."

It may not appear at first sight to matter much whether the trade of a country is based upon one metal or another. Economic history shows clearly, however, that the silver basis is far inferior to the gold basis, just as it shows clearly that the gold basis is inferior to the free credit basis.

In the Middle Ages when a horse cost only ten shillings it was almost as convenient to buy a horse with silver as with gold. When sheep cost fourpence a groat was a more convenient coin than a half-sovereign. With increased industrialisation silver rapidly lost its convenience. Everyone has found how very cumbrous a piece of currency the crown or the dollar is. A single crown is inconvenient in one's pocket. To purchase a horse in 1910 for £50 in gold was a reasonably convenient operation, though less so than to purchase it in banknotes. To carry through the purchase in five-shilling pieces would have been most inconvenient. What is true in the individual transaction is true of the national trade. No country upon a silver basis could compete with one on a gold basis, and as soon as Germany made the change she commenced to challenge British supremacy. Her example was soon followed by other countries, in which gold became the recognised basis of commerce, though it may

not even yet have received complete legal recognition.*

The adoption of gold as a trade basis by the world at large has resulted, naturally enough, in increasing the strain upon gold. The restricted credit system of centripetal finance rests, be it reiterated, upon the economic heresy of allowing no instrument of equal or greater circulating power to compete freely with gold. The result is to build up a whole mass of non-circulating instruments (cheques, bills of exchange, stocks, shares, bonds, etc.) upon the centralised gold reserve in order to carry on industry. In every industrialised community this strain upon gold has proved too great, and natural relief is sought in lessening the strain by limiting the credit over-structure, and by strengthening the centralised gold reserve. The unfortunate effect of this has been to starve agriculture, to reduce the effective demand for goods, to promote unemployment and underpaid employment, and to exclude all except the favoured inner circle from a share in credit facilities. The credit structure being unsound and insufficient, competition must be avoided or curtailed.

The method of reducing competition internally by refusal of credit is not the only means available. Another means is obviously to keep out competition from abroad. To this cause can be

* See p. 146.

traced the increasing drift towards Protection and higher tariff walls since 1873.*

The question of dumping is one which figures largely in the tariff controversy. It is regarded as an unfair method of trading. The doctrinaire Free Trade refuses to admit its existence, alleging that no foreign trader would wilfully sell below a profitable price. The Tariff Reformer cites case after case of foreign goods being sold at an unduly low price, with the intention of ousting the home goods made from the market. The dislike of dumping as a trade practice has done a great deal to foster international animosity. The British worker resents the prospect of unemployment due to cheaper foreign goods closing the market against him. Nevertheless, international trade follows the same lines as internal trade. Underselling one's rival at home is a fair trade method if the rivals are on even terms. Where, however, one of the rivals has undue control of credit resources the rivalry ceases to be fair. The methods by which the National Cash Registry Co. of America ousted its rivals from business are typical and are worthy of the closest study.† The

* Tickner, p. 618: "Since 1873 there has also been a decided reaction on the part of European nations towards a policy of protection by means of tariff."

† See Ripley, pp. 672-702. One method cited has at least the merit of being picturesque. "A display-room was maintained in the factory at Dayton, known as the 'Graveyard,' wherein were

competition in that case was against other American firms, and though it caused discontent did not aggravate international friction. When, however, a foreigner unfairly undercuts the home market the discontent is likely to become inflamed into a national hate.

All dumping does not proceed from a malicious attempt to oust rivals. It is more often an innocent method of self-preservation. In internal trade, during a period of credit stringency, many firms are obliged to obtain cash resources by selling their articles below cost price. But during such a period there is very little purchasing power in the country. The result is a tendency to sell abroad, where purchasing power is more ample. Such a proceeding is being indulged in to-day. The nations of Europe that are starving for credit are selling their commodities regardless of cost to enable themselves to carry on over what is thought to be merely a temporary crisis. Purchasing power being absent inside the country owing to the credit shortage, they are selling to Great Britain and to America. Pre-

exhibited all the machines which had been 'knocked out.' Cards were attached to each register, giving dates, amount of money lost, and similar discouraging information. This was a prominent feature of the intimidation programme. Obstinate competitors were invited to visit Dayton, and were escorted through this gruesome exhibit."

war dumping was but a less intense degree of the same proceeding.

The return of Great Britain to a protective tariff after some eighty years of Manchesterian Free Trade will come as a bitter blow to the *laissez-faire* school. The tendency is, however, plainly in evidence. One important factor, which may prove to be the determining one, has recently come into operation. Before the war the greatest antagonist of Protection were the banks, who did not feel the pinch of competition. The United States Federal Reserve Act (December 23, 1913) allowed the National banks with capital of more than $M1 to open branches in Europe. The result is that American banks are now trading in England, and are making great strides.*

With the greater credit resources of America behind them and with their more enterprising methods, it is probable that they will prove dangerous rivals.

* According to the *Economist*, vol. xci., No. 4,026, Banking Number October 23, 1920, p. 660, only one bank has taken advantage of the Act, four trust companies having already had offices in London. "The list has been added to this year by the advent of the National City Bank of New York. . . . This is a substantial concern. Moreover, it is progressive, and has been extending its operations during the year to various quarters of the world." It has now two branches in London (Waterloo Place and Bishopsgate). The Guarantee Trust Company of New York opened two additional branches in London in 1920-21, and a second in Liverpool in April, 1921.

The Free Trade gospel has failed to realise the hopes which it inspired. It did not greatly improve the lot of the worker. The difference between the conditions of life in Free Trade Britain and the protected countries is not appreciable. The reason lies not in the falsity of the Free Trade principle, but in the fact that Britain has never been a Free Trade country. The offspring born of the unnatural union of freedom in industry and State control of finance has proved a disappointment to its sponsors. The half-caste is no better than the nigger.

The decline of Free Trade might be a thing to deplore but for the fact that the gospel was false to itself and deserves the fate that awaits it. A gospel that advocates freedom in exchange, yet condones, or even supports and furthers control of credit, the vehicle of modern exchange, is a lie unto itself. Its downfall will clear the ground for a better understanding of the real problem.

Aggressive financialism is the most disruptive force in modern society. Its genesis was naturally at the centre of the centripetal system, in the north-eastern part of the United States, east of the Mississippi and north of the Potomac. Its methods are attracting a great amount of examination. The extraordinary accusations of a Boston

financier* might be ignored as savouring of the melodramatic were they not reinforced by the more balanced judgment of later investigators. Aggressive financialism is non-moral and non-scrupulous. It has corrupted legislature, it has influenced courts of justice. The legal palliation of the action of the Morgan pool in the matter of the United States Steel Corporation, and the court's condemnation of the public-spirited plaintiff, has been entirely reversed by the moral verdict of the community.† The influence of the financial pool over the United States Treasury was demonstrated in the 1907 crisis, when a Secretary of State was obliged to recognise the Morgan interests as being in supreme control. Now the financial pool is threatening to do openly what it has hitherto accomplished indirectly. The financial interests are supreme, and the political machine must work at their command.‡

* Lawson, p. vii.: "During the last twenty years there has grown up in this country a set of colossal corporations in which unmeasured success and continued immunity from punishment have bred an insolent disregard of law, of common morality, and of public and private right, together with a grim determination to hold on to, at all hazards, the great possessions they have gulped or captured."

† See Ripley, p. 256.

‡ President Wilson, p. 157: "We have been dreading all along the time when the combined power of high finance would be greater than the power of the Government. Have we come to the time when the President of the United States or any man who wishes to be President must doff his cap in the presence of this high finance?"

While it was merely a question of the internal control of power in America the world might look on with a detached gaze. The contest has passed into a further stage. The Morgan pool not only dominates America, it is attempting to dominate the world. The recognition of Mexico is said to be bound up with the creation of an official bank upon the lines of the Federal Reserve banks, with the control in the hands of American banks,* who are in turn controlled by the Morgan pool. Trade competition with Europe threatens to become aggressive. Whether it will be upon recognised commercial lines, or whether political influence will be used, remains to be seen. The danger is but dimly realised, yet the British Ambassador has already indicated it.†

Let us face the facts squarely. Centripetal finance has contributed to reduce Ireland from a prosperous to a discontented country, and to make it a constant source of friction in international affairs. Centripetal finance has given the oil control of the

* See *Financier*, November 16, 1920, article by Leopold Grahame.

† Speaking at Minneapolis on November 5, 1920, Sir Auckland Geddes said: "America and Great Britain must avoid national trade competition organised by the Government and supported by political action." Otherwise "there would inevitably come a clash of interest that would at least strain the friendly relations between the two countries" (see *Financier*, November 6, 1920).

world over to two competing groups. The Standard Oil Company is linked with the Morgan interests. The onset of the fight for mastery will occur in Mexico which the Standard Oil Company's interests intend to control through the Federal Banking system. Centripetal finance has erected tariff walls, has caused credit starvation throughout Europe. It has brought the economic system to the verge of complete collapse, and the more militant financial interests are preparing for the fight for complete control of the world's destiny.

What remedy has been proposed for the evils under which the world is suffering? Economic congresses have gathered and discussed. Public-spirited individuals have set forth their views. From among the many discordant views there is one which grows steadily in volume. It is to the effect that the world shall be supplied with credit by an international commission of financiers who shall be free from political influence. Reading into the empty phrase the underlying meaning of the proposal, it results in nothing less than the suggestion that the destinies of mankind shall be handed over to a group of individuals, the dominant personalities of which shall be members of the Morgan pool.

This, then, is the end of progress. Centuries of struggle have enabled us to escape from a condition of feudal servitude, based upon a claim to land, to

yoke ourselves under a financial servitude, based upon a claim to gold. The feudal overlord was the king, and his title was hereditary. The financial overlord wears no crown, but his power descends by testament. Morganism is already in its third generation. One hereditary tyranny has been replaced by another. Hohenzollerns and Romanoffs are an anachronism, financial despots are our accepted monarchs.

The outcast of the feudal period was the lordless man who could not attach himself to a territorial master, who wandered about without a claim to any lot of ground that he could till. To-day the outcast is the wageless man who cannot attach himself to a financial lord, who can secure no claim upon the world's cash resources, a mere unit in the vast army of unemployed.

Another remedy is mooted. It is violently to overturn the whole economic machine, in the hope that somehow or other a better system will emerge. No responsible persons father such a doctrine, yet the talk of revolution is current to an increasing extent. That the revolutionaries are agitators may be true, yet their existence in our midst is undoubted.

Man must find an outlet for his energies in some channel or another. If he can apply those energies constructively he will usually do so. If he cannot,

he will divert them to destructive ends. The present system affords insufficient outlet for the pent-up energies of the individual upon constructive lines. Isolated persons may be pointed out whose extraordinary abilities or good fortune have enabled them to elevate themselves to commanding positions. Here and there a rare success may be found, but the evident fact of life is that out of every twenty human beings nineteen at least are condemned by the present system to remain in the state of poverty to which they were born or to sink lower in the scale. The cases of success are all too rare to provide a safety factor sufficiently ample for the community's needs. The enterprising, more forceful artisan has not sufficient hope of success by constructive energy. He diverts his will and his intelligence from the production of wealth for absentee owners, and he applies them to barren agitation. How constructive he remains in spite of all is shown by the huge movement which the working-class agitators have built up. The Trade Union movement is a monument to misspent effort. Constructive in its organising ability, it is negative or destructive in its economic methods. Trade Unions afford no sufficient outlet for the progressive type of workman, and both within them and outside them the extreme destructive type is gaining ground.

That revolution should be considered, by even a

small section of the nation, as a method of achieving progress is an indication of the mental and economic impasse at which we have arrived. The idea would be unthinkable had we not before us the spectacle of the most populous and most docile European nation continuing in the revolutionary faith after three years of economic failure and centralised despotism. The unpent liberalising forces of the Russian people have been soured into callous and calculated repression of liberty by the failure of Sovietism to evolve a system of credit upon which the economic machine would continue to function.

From the welter of confusion one truth clearly detaches itself. A revolution resolves itself finally into a struggle for food. The industrial system breaks down, credit disappears, and the primeval pursuit of agriculture alone remains. The struggle changes its aspect. It is no longer one between political despotism and liberty, it is one between town and country, between population and food supply. In Russia, where almost the whole of the population could live upon the food supply, the struggle has been at its minimum. Yet the towns are depopulated and its country-side famine-stricken.

A revolution in England would mean what it has meant in Russia, but the struggle would be at its intensest. England is the most industrialised

community of the world. Its town population is in greater proportion to the whole than that of any other country. Its country-side is hardly in England at all. The chief sources of its food are across the ocean. The disruption of the credit system which would follow upon a revolution in England would mean the starvation of the urban population.

Neither of the above indicated remedies influences the general mass of the community. The appointment of a financial world-cabinet is unnecessary. Such a body already exists in embryo, and its members direct the world's destiny. Its constitution will become more clearly defined as the centripetal rays are brought to one focus. The revolutionary method is scouted by the people. Revolutions come not from the conscious will of a whole people, but from the impingement of a strong disruptive influence upon the mass of general discontent.

The only other remedy urged is the healing influence of time. The hope stimulates the thought that things will right themselves. Peoples will settle down after the war's ravages to the contentment of pre-war days. The pious hope that inspires this optimism is not based upon reason, but upon an innate desire to avoid facing unpleasant facts. Aggressive financialism, intensified nationalism, commercial jealousy, trustification, the struggle for markets, disparity of wealth, the spectre of un-

employment, squalor, hopelessness, and violence—these were not diminishing but increasing symptoms of industrialised life in pre-war days. The same cause which produced racial wars and individual destitution will operate in the future to a greater degree than in the past unless the system is changed.

Already there is a re-forming of national interests, a re-shaping of political forces. Secret alliances and understandings are being promoted. Causes of friction between old enemies and recent allies are observable on all hands. The blind optimism which refused to admit the possibility of the last war will refuse to consider the probability of the next one. It will not allow itself to see that nations are plunging into poverty. It will lull itself into repose by urging the necessity for retrenchment of public expenditure, regardless of the fact that no political party dares to reduce its commitments to pre-war level, that three-fourths of the nations of Europe show a deficit in their annual budget. Blind optimism will hope for the best, but it will provide no remedy against the worst.

There is one remedy. The system which has brought us to the edge of complete disaster must be altered. Artificial centripetalism must give place to a natural centrifugalism. Control of finance must yield to free competition in credit. The call

on gold as a basis of industry must be supplanted by the claim to real wealth.

The world needs not despotism nor revolution but progress. The path of progress is clearly marked out by a study of economics, the doctrine of the professor and the Socialist notwithstanding. The removal of State restrictions will allow a gradual growth of the note-issuing bank. The volume of notes will increase and decrease, not in accord with the preconceived fancies of politicians, but in accord with the needs of the community. They will be based, not upon debt or negative wealth, but upon production or positive wealth.

With the reversal of the financial system, the pools, the trusts, the limited companies will disappear. The creditable individual will obtain credit facilities to initiate enterprise. The banker will be, not the hoarder of gold, but the credit specialist. The change will not be abrupt, but gradual; not disruptive, but progressive. The marginal differentiation which has worked in favour of the possessors of the call upon gold will, under a free system, work in favour of the possessors of creative ability. The gold basis will remain only as long as it is of use to the community. When the competing banks have proved their worth and have provided the community with credit instruments of proved value, the community will desire less and

less to have recourse to the gold reserve to test the value of the note. The increasing wealth of the community will form the basis of more ample credit. The smaller producer will be able to compete on an equality with the larger producer. The workman will find employment at a just wage, and will have an open avenue to ascend to that position in the social system to which his constructive ability and his productive capacity entitle him.

Nationalism will become a decreasing factor in the world's affairs. Bureaucracies will diminish because a commercial career will offer better scope than a non-productive official life. The agitator will find a lessening sphere in the growing content.

The rate of usury will decline, and the incentive to use one's saved wealth in one's own business will increase. The tendency towards occupying ownership of land will re-establish itself. The lease-tenure of land will become of longer and longer duration, and the rents paid to absentee landlords smaller and smaller.

Economics will be placed upon a proper footing. It will become a study of wealth, not of poverty. The repudiation of the heresy of State control of credit will place the science upon its true basis. The notion that the centralisation of credit resources could, in any possible way, lead to the diffusion of wealth is not only the antithesis of scientific thought,

it is a contradiction of every form of horse sense.

Mass tyranny must be admitted to be a necessary evil. It will become a lessening factor in social life when the economic pressure is removed. Minorities may have to suffer to some extent, but the suffering will decrease, instead of increasing as at present. Majority rule may remain as the ultimate court of appeal, but its jurisdiction will be gradually curtailed.

Compulsory organisation will give place to voluntary association. No longer will the worker be forced to join a powerful union or risk ostracism by his fellows. When the industrial system allows a free outlet for productive energy, the need for the coercive tyranny of trade-unions will disappear. A better outlook will await the worker than that of being a trade-union conscript, to be offered up at intervals as strike fodder.

The economic involution of the present time will give place to a natural economic evolution. The tyranny of the controllers of industry will dwindle when state control of credit has passed out of the economic organism.

The path of progress will be straight and the course of progress even. Society will recognise that the unit of progress is not a political caucus or a coercive corporation, but the constructive individual

free to work out his own salvation either alone or in such forms of voluntary association as may prove their usefulness.

The problem has been stated and the solution shown. On the one hand we have bankruptcy, despotism and poverty: bankruptcy of credit, of industry, of reform; despotism of financial overlords and their political minions; a permanent pauperisation of the workers, and an increasing impoverishment of the technical classes; a subordination of the inventor, the organiser, the producer, to the absentee owners of paper bonds. On the other hand we have the promise of financial stability and credit expansion: encouragement to the enterprising, a fair wage to the worker, economic progress and individual freedom, a decline of national separatism, of military and financial aggression.

THE CHOICE IS BEFORE THE WORLD:
THE WORLD MUST CHOOSE.

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